Higher One Holdings, Inc.
Form 10-K
February 24, 2011
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

FOR ANNUAL AND TRANSITION REPORTS PURSUANT TO

SECTIONS 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

(Mark One)

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

For the fiscal year ended December 31, 2010

or

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

Commission file number: 001-34779

Higher One Holdings, Inc.

(Exact name of Registrant as Specified in Its Charter)

Delaware	**26-3025501**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**

25 Science Park

New Haven, CT 06511

(Address of Principal Executive Offices, Including Zip Code)

203-776-7776

(Registrant s Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(b) of the Act: Common Stock, par value $0.001

Name of exchange on which registered: New York Stock Exchange

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

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

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 x

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

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

Indicate by check mark 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. x

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. (Check one):

Large accelerated filer	¨	Accelerated filer	¨
Non-accelerated filer	x (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 Exchange Act). Yes ¨ No x

The aggregate market value of the registrant s common equity held by non-affiliates based upon the last sale price of the common equity reported on the New York Stock Exchange on June 30, 2010, was approximately $806,774,012.

There were 56,371,141 shares of the registrant s common stock outstanding as of February 18, 2011.

DOCUMENTS INCORPORATED BY REFERENCE:

None.

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HIGHER ONE HOLDINGS, INC.

YEAR 2010

FORM 10-K ANNUAL REPORT

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FORWARD-LOOKING INFORMATION

This annual report on Form 10-K contains forward-looking statements. For this purpose, any statements contained herein that are not statements of historical fact may be deemed to be forward-looking statements. Without limiting the foregoing, the words believes , anticipates , plans , expects , should and similar expressions are intended to identify forward-looking statements. The factors discussed under Item 1A. Risk Factors , among others, could cause actual results to differ materially from those indicated by forward-looking statements made herein and presented elsewhere by management from time to time. We expressly disclaim any obligation to update or alter our forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

We use the terms the Company , we , us and our in this annual report to refer to Higher One Holdings, Inc. and its subsidiaries, unless the contex requires otherwise.

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PART I

Item 1. Business

We are a leading provider of technology and payment services to the higher education industry. We believe, based on our experience in the industry, that we provide the most comprehensive suite of disbursement and payment solutions specifically designed for higher education institutions and their students. We also provide campus communities with convenient and student-oriented banking services, which include extensive user-friendly features.

The disbursement of financial aid and other refunds to students is a highly regulated, resource-consuming and recurrent obligation of higher education institutions. The student disbursement process remains mainly paper-based, costly and inefficient at most higher education institutions. These institutions are facing increasing pressure to improve administrative efficiency and the quality of service provided to students, to streamline regulatory compliance in respect of financial aid refunds, and to reduce expenses.

We believe our products provide significant benefits to both higher education institutions as well as their campus communities, including students. For our higher education institution customers, we offer our OneDisburse® Refund Management® disbursement service. Our disbursement service facilitates financial aid and other refunds to students, while simultaneously enhancing the ability of our higher education institutional clients to comply with the federal regulations applicable to financial aid transactions. By using our refund disbursement solutions, our clients save on the cost of handling disbursements, improve related business processes, increase the speed with which students receive their refunds and ensure compliance with applicable regulations.

For students and other campus community members, we offer our OneAccount service that includes a Federal Deposit Insurance Corporation, or FDIC,-insured deposit account provided by our bank partner, OneCard, which is a debit MasterCard® ATM card, and other retail banking services. OneAccount is cost competitive and tailored to the campus communities that we serve, providing students with convenient and faster access to disbursement funds.

We also offer payment transaction services which are primarily software-as-a-service solutions that facilitate electronic payment transactions allowing higher education institutions to receive easy and cost effective electronic payments from students, parents and others for essential education-related financial transactions. Features of our payment services include online bill presentment and online payment capabilities for tuition and other fees.

Higher One, Inc. was founded in 2000 in New Haven, Connecticut by Mark Volchek, Miles Lasater and Sean Glass. In July 2008, Higher One, Inc. formed Higher One Holdings, Inc., which is now the holding company for all of our operations. Higher One Holdings, Inc. is incorporated in the state of Delaware.

Our Strategy

We believe that there is a significant opportunity to continue to achieve significant future growth. We intend to continue to increase revenue and profitability by strengthening our position as a leading provider of technology and payment services to the higher education industry. Key elements of our growth strategy include:

- Expanding the number of contracted higher education institutions;
- Increasing OneAccount usage;
- Cross-selling our existing products and services;
- Enhancing and extending our products and services; and

Pursuing strategic partnerships and opportunistic acquisitions.

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Products and Services

We provide products and services to two distinct, but related target markets: higher education institutions and their students.

Products and Services for Higher Education Institutions

We provide our higher education institutional clients with an integrated suite of products and services. These include our OneDisburse® service, our payment suite and other financial services.

OneDisburse®

Our OneDisburse® Refund Management® product is a turnkey solution that provides higher education institution clients with a comprehensive technology service for streamlining the student refund disbursement process. Following the payment of their tuition and other school-related expenses, many students receive residual financial aid disbursements to cover non-academic school expenses, such as living expenses and books. Students also receive disbursements, such as a refund following withdrawal from a course or other miscellaneous fees. Higher education institutions have typically processed these refund disbursements by preparing and distributing paper checks, which is both time consuming and costly for institutions and slow and inconvenient for students. After a higher education institution purchases the OneDisburse® service, the institution sends the full amount of each student s disbursement to us and we then forward the funds to the student in accordance with the student s instructions. For students with OneAccounts, disbursements are generally made by electronic transfers to their OneAccounts. By partnering with us to provide refund disbursements and related processes, including the student/customer service function, our clients reduce their time and cost spent on handling disbursements, improve the related business processes and increase convenience for students. In addition to saving time and costs for our clients, OneDisburse® is designed to ensure that the refund disbursement process is fully compliant with all applicable federal regulations, thereby providing our clients compliance monitoring services, which eases their administrative and regulatory burden. OneDisburse® also has a number of features that benefit students receiving refunds, including convenient and fast processing of refunds and notifications via email or text message of incoming refund disbursements. As of December 31, 2010, over 430 campuses serving approximately 3.3 million students had contracted to use the OneDisburse® service.

Payment Suite

Our payment suite includes the following software-as-a-service products and services, which our higher education institutional clients may purchase separately or together as a bundle. As of December 31, 2010, over 330 campuses serving approximately 2.5 million students had contracted to use one or more products and services in our payment suite.

ePayment . Our ePayment product enables higher education institutions to securely accept online payments for tuition, charges and fees from students via credit card, pinless debit or without charge via ACH. Our ePayment product also allows students to set up and maintain recurring payments and authorize other users such as parents to pay student related charges on their behalf. SmartPay, a feature of ePayment, enables higher education institutions to reduce the cost of accepting credit and debit cards by passing the convenience fee to the payers.

eBill . Our eBill product enables higher education institutions to automate payer billing and processing functions performed on campus and to extend payment services. This product allows the student or authorized payer to view the bill online and enables them to make payments online. By automating the billing process and facilitating electronic payments, higher education institutions can reduce administrative and labor costs, deliver bills quickly and securely and increase student and authorized payer convenience. eBill also expedites the processing, authorization and receipt of student payments.

MyPaymentPlan . Our MyPaymentPlan product enables higher education institutions to

personalize students payment plans, in order to better meet the individual needs of each student. In particular, MyPaymentPlan offers campus administrators the ability to tailor payment plan rules and fees; access the status and history of each student s account; and calculate the due date and payment schedule for each student.

eMarket . Our eMarket product enables higher education institutions to provide their academic, athletic and other departments with Internet e-commerce storefronts that can be used for, among other things, taking alumni donations, selling items such as event tickets, t-shirts and other merchandise, and accepting payments of event and conference registration fees. Higher education institutions can also use eMarket as an administrative portal to maintain centralized control of policy setting and reporting while allowing individual departments and entities autonomy to manage their operations. This centralized approach enables the institution to update policies related to campus commerce immediately and uniformly throughout all departmental campus storefronts.

Cashiering . Our Cashiering enables higher education institutions to operate and manage their cashiering functions, back office payments and campus-wide departmental deposits. In particular, Cashiering allows: institutions to process walk-in and mail payments at any cashier s office on campus; departments to allocate deposits to specific general ledger accounts in a paperless environment; and multiple locations to receive any information that is downloaded into the CASHNet database.

Other Products and Services

OneDisburse® ID. We offer our higher education institutional clients the option to combine our debit card with the institution s ID cards. If an institution elects this option, we provide its students with our OneCard, which is a debit MasterCard ATM card and also serves as their official campus identification.

OneDisburse® Payroll. Our OneDisburse® Payroll product can quickly and efficiently distribute payroll and other employee-related payments through the OneDisburse® platform.

Financial Intelligence. In 2009, we launched a product to deliver financial literacy to the students at higher education institutions that can be purchased by the institution and offered directly to students through their existing Higher One co-branded website. This product offers students an online class that uses game based learning to help teach financial literacy.

Products and Services for Students The OneAccount

Through our bank partner, our OneAccount product provides students, as well as faculty, staff and alumni, with an FDIC-insured online checking account with no monthly fee and no minimum balance. We also provide OneAccount holders with a OneCard, which is a debit MasterCard ATM card. Students can use their OneCard instead of cash or writing checks to make purchases wherever MasterCard is accepted at millions of locations worldwide or online. Many students also use their OneCard to pay bills automatically, send money instantly to other OneAccount holders and access over 540 Higher One ATMs located on or near campuses, with no fee to OneCard holders.

The OneAccount includes features designed to provide students with powerful, convenient, user-friendly tools to manage their finances, such as free text to balance, mobile low balance alerts, a mobile website and a scan deposit feature. Other customized features of the OneAccount include: Campus Auto-Load, which allows students to set up automatic funds transfers to campus flexible spending accounts, and the Request Money and Send Money features, which allow students to request money from parents and provides parents with a mechanism to make person-to-person payments into students OneAccounts, respectively. As of December 31, 2010, there were approximately 1.6 million OneAccounts. In December 2010, we began to offer a new version of the OneAccount, that has a different fee schedule compared to the original OneAccount. We may offer other versions of the OneAccount in the future as well. Different versions of the OneAccount either have or are expected to

have different fee schedules, some with monthly fees that are waived if certain activity requirements are met.

Sales and Marketing

Our sales and marketing efforts separately target our two key markets: higher education institutions and their students.

Higher Education Institutions

Our dedicated and experienced sales team actively markets our products and services to higher education institutions in the United States. This team identifies potential new clients through a variety of channels, including higher education regional and national tradeshows, existing client showcase events and through word-of-mouth referrals. The sales process typically includes an extended solicitation period, which can be lengthy, and that usually includes phone conversations, in-person presentations and formal proposals to various levels of administrators. Historically, our primary points of contact have been an institution s chief financial officer and bursar; however, following our acquisitions of EduCard LLC, or EduCard, and Informed Decisions Corp., or IDC, our marketing team also started contacting chief technology officers.

An important part of our sales effort is educating our potential clients about the benefits of our products and services for both the higher education institution and its students. Institutions generally are attracted to the idea of partnering with us to provide their payment functions because of the resulting operating efficiencies, compliance monitoring and the potential benefits to students, such as receiving financial aid disbursements and paying bills more quickly and conveniently.

Students

Once we enter into a contract with a higher education institution, we begin focusing our marketing effort on the institution s students. Our consumer-marketing department conducts student-directed marketing efforts with a primary goal of increasing awareness and usage of our services, including both our payment products and our OneAccount.

We work closely with our higher education institutional clients to communicate the benefits of our products and services through school-branded communications and literature in an effort to increase both the number of new OneAccounts and usage of existing OneAccounts. Typically, we will send information to parents and incoming students soon after their admission applications are accepted by the school and during student orientation. We generally contact returning students before the beginning of a new semester and place signs in strategic campus locations such as bookstores, student centers, dining halls, athletic facilities and cash dispensers to increase awareness of our products and services. Before we introduce our OneDisburse® service to a new higher education institutional client, we frequently implement a word of mouth program through which selected students volunteer to use our service and provide word of mouth marketing and education to other students on campus. In an effort to strengthen our relationships with students, we often sponsor and support on-campus events and create a co-branded website with the higher education institutions. Our higher education institutional clients provide us with student email addresses that we commonly use to communicate with students about our products and services. Many times, we also use these email addresses, as well as on-campus orientation events, to distribute our Money 101 lessons, which provide tips and other information to improve students financial literacy, such as explaining how a checking account works, how to protect against security breaches and how to avoid excessive fees.

Customer and Client Service

We are dedicated to addressing the needs of both our higher education institutional clients and student customers. We believe that our multi-pronged approach to providing cost-effective customer service helps make us an industry-leader in customer satisfaction.

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Higher Education Institutions

We believe we enhance our sales and marketing efforts by providing reliable after-sale service. Our dedicated client-service employees are focused on servicing our higher education institutional clients.

We provide higher education institutional clients with a variety of service touch points, such as a dedicated relationship manager, OneSupport, our client support for managers and administrative staff at our higher education institutions, and the Higher One User Group, or HUG, our regularly held client conference. Our dedicated relationship managers are responsible for ensuring we maintain a strong relationship with each of our institutional clients and for assisting, supporting and providing updates on the quality and use of our services. OneSupport is designed to address a range of client issues from client specific technical questions to client service matters that require management s attention. During our HUG conferences, clients can meet in-person with our management and staff to learn about new features and products, updates to current offerings and build long lasting personal relationships.

Students

As of December 31, 2010, we had approximately 190 after-sales customer service representatives to assist students and others in the campus community that use our products and services. Our website provides a searchable database of frequently asked questions that we regularly update as more questions are answered by our customer service team. This database helps us assist our self-service oriented customers. We also provide students with the ability to contact us via telephone, email and text message.

We systematically evaluate our performance through our analysis based on our internal service levels established for customer service inquiries and response and issue resolution times. We also record and analyze refund delivery cycles and seasonal variances to help identify and adapt to particularly high volume periods by, among other things, increasing ATM cash holdings for peak refund periods and increasing customer service staff during seasonally busy periods, which is typically the beginning of each semester.

Key Relationships with Third Parties

We maintain relationships with a number of third parties that provide key services for us. By partnering with third-party providers, we are able to streamline our own operations and infrastructure and provide a high level of specialized services. Our primary third-party provider relationships are with the following entities:

The Bancorp Bank

The Bancorp Bank provides FDIC-insured depository services for all of our OneAccounts, as well as other banking functions such as supplying cash for our ATM machines. Under the terms of our agreement with The Bancorp Bank, we maintain responsibility for the technology-related aspects of the OneAccounts.

The Bancorp Bank is a publicly traded, Delaware-chartered, FDIC-insured depository institution. We began our relationship with The Bancorp Bank in May 2008 and our current agreement is scheduled to expire in May 2013. It will thereafter automatically renew on an annual basis unless either party cancels. We have a right, subject to a notice period, to terminate this agreement. Upon termination of the agreement, The Bancorp Bank is obligated to transfer the OneAccount deposits to another institution that we designate. We do not pay The Bancorp Bank a fee for its services; rather its sole compensation is to retain the investment returns earned on OneAccount deposits. The Bancorp Bank pays us a monthly processing fee based on amounts deposited in OneAccounts and prevailing interest rates.

The market for FDIC-insured retail banking services is very competitive and we continue to evaluate other bank partnership options. While we are satisfied with our current bank partnership, we believe other options would exist if we changed partners. The Bancorp Bank is our third banking partner since our inception and, in the past, when we have changed banking partners, we have done so in a

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limited amount of time and with no material disruption or inconvenience to any of our customers. While we have evaluated the relative costs and benefits of establishing or acquiring an institution capable of offering FDIC-insured retail banking services, we have decided to operate our banking activity through a bank partnership at this time for strategic and operational purposes.

Fiserv Solutions, Inc.

Fiserv Solutions, Inc., or Fiserv, provides back-end account and transaction data processing for OneAccounts and OneCards, including: core processing, ACH processing, issuance authorization and settlement, ATM driving and related services. We began our relationship with Fiserv in November 2001 and our current agreement is scheduled to expire in June 2014. Thereafter, unless either party cancels, our agreement will automatically renew on an annual basis. We pay Fiserv a monthly fee for services rendered and related software licenses.

MasterCard International Incorporated

MasterCard International Incorporated, or MasterCard, provides the payment network for our OneCard MasterCard debit and ATM card and certain other transactions, including for SmartPay. We have an exclusive relationship with MasterCard through 2013 for the issuance and marketing of debit cards. As a registered member service provider with MasterCard, we arrange for the marketing of both embossed and unadorned MasterCard debit cards. Fiserv is a principal debit licensee of MasterCard and provides certain processing, implementing and support services to facilitate our OneCard program. We receive various incentives, both directly from MasterCard and indirectly through Fiserv, for achieving growth targets in the issuance and promotion of our cards.

Comerica Incorporated and Global Payments Inc.

Comerica Incorporated and Global Payments Inc., or Comerica and Global Payments, provide transaction processing and banking services for payment processing related to the SmartPay feature of our ePayment service. The primary function of Global Payments is to route credit card authorization requests and to settle credit card transactions. Comerica provides acquiring sponsorship in the card payment networks related to our SmartPay service.

Terremark North America, Inc. and Neospire, Inc.

Terremark North America, Inc. (*formerly NAP of the Americas, Inc.*), or Terremark, and Neospire, Inc., or Neospire, provide web and application hosting services in secure data centers. These vendors provide various managed services including security, network, cooling, power, hardware and other services to host our proprietary applications. Both vendors have been certified as compliant with Payment Card Industry s, or PCI, standards and have business continuity plans. Under our standing agreement, we occasionally purchase computer hardware and software from Terremark and Neospire. We also compensate Terremark and Neospire on a monthly basis for services rendered.

Technology

We have invested in establishing a secure technology platform to provide us with a flexible and scalable infrastructure. Our technology strategy is to focus our internal resources on proprietary applications while leveraging third party partnerships or purchases for more routine applications. For example, the OneDisburse® and OneAccount platforms include major components of internally developed software, while we partner with third parties to provide banking core processing, transaction processing and web hosting.

The key modules of our technology platform include:

HigherOneAccount.com

Our software engineering team has developed and maintains this web application, which allows students and parents to manage their OneAccount. It offers robust, self-service online banking for our

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OneAccount accountholders including: viewing statements, paying bills, making electronic deposits, making electronic transfers and filing service requests. It also integrates institution-specific features, including management of payroll, financial aid refunds and automatic replenishment of campus accounts through Campus Auto-Load. This website also allows attractive opportunities for co-branding with our higher education institutional clients.

CashNet.com

This web application is used to administer and initiate transactions in our payment suite of products. Higher education institution administrators can change certain confirmation settings and run reports, while students and parents can perform certain functions, such as viewing electronic bills, making payments and enrolling in payment plans.

HigherOneSupport.com

We maintain this administrative website for use by our higher education institutional clients and our internal staff. It offers institutions useful functions, including real-time reports, research on cards and students, access control for administrators to the website and an audit trail of all cash movement. Our internal staff performs customer service, transaction flow monitoring, access control for employees and site administration for this website.

HigherLink

HigherLink is our batch file processing engine for integrating our technology with the systems of our higher education institutional clients and other external parties. It handles import and processing of cardholder demographic data, photos and disbursement files, as well as export of card status files and other integration files.

Technology Audits

Our development team, consisting of both in-house and third party contractor team members, develops and tests our proprietary software applications, including our regular software releases. Since 2006, we have conducted technology audits that are designed to identify weaknesses in our information technology infrastructure and to provide recommendations for how to improve it. We incorporate the audit findings into our strategic planning process.

Our CASHNet® payment suite was most recently certified as PCI-compliant in January 2011 by 403 Labs. Each of our critical systems, other than our customer service call center, has internal redundancy functions and often includes secondary sites. While our customer service representatives are geographically dispersed, the customer service related telephone system housed in our New Haven, Connecticut office must be functioning to keep customer service phone lines open. In order to reduce the risk of our customer service representatives losing the ability to take live inbound calls, we are in the process of creating a secondary site for our telephone system.

Intellectual Property

We rely on a combination of patent, copyright, trademark and trade secret laws, as well as nondisclosure agreements and other agreements and technical measures to protect our technology and intellectual property rights, including our proprietary software.

We have four registered patents and several patent applications in the United States relating to our products and services. In addition, we use a variety of unregistered trademarks and have seven registered trademarks in the United States: Higher One®, OneDisburse®, Refund Management®, CASHNet®, CASHNet (service mark)®, CASHNet any payment, anytime, anywhere® and CASHNet Business Office®. Our domain names include HigherOne.com, HigherOneSupport.com, HigherOneAccount.com and CASHNet.com and our proprietary software includes both internal and customer facing applications. See Part I, Item 1. Business Technology of this report. Finally, we also license certain intellectual property from third parties.

Our issued patents expire in 2023 and 2024. Our trademark registrations have various expiration dates, but, subject to applicable law at the time, our trademark registrations generally can be renewed or otherwise extended on an ongoing basis based on proper use and formal renewals.

Although our business is not dependent on any single item of our intellectual property portfolio, and no item of our intellectual property is material to the operation of our business, we believe that our intellectual property provides a competitive advantage, and from time to time we have taken steps to enforce our intellectual property rights. See Part I, Item 3. Legal Proceedings of this report.

Competition

We do not believe there is a competitor that provides a suite of products and services to the higher education industry that is as comprehensive, integrated and tailored as ours. However, the market for payment services in the higher education industry is competitive. Other companies, including SLM Corporation (Sallie Mae®), Nelnet, Inc., PNC Financial Services Group, Inc. and TouchNet Information Systems, Inc., provide payment software, products and services that are competitive to those that we offer. For student banking and debit card services, we compete with banks active in the higher education industry, including U.S. Bancorp and Wells Fargo & Company.

While many of our competitors have substantially greater financial and other resources than we have, may in the future offer a wider range of products and services and may use advertising and marketing strategies that achieve broader brand recognition, we believe that our products and services remain competitive in their respective markets. In particular, we believe that the functionality and service provided by our OneDisburse® and payment suite of products provide us with a competitive advantage, while the pricing of, and services provided for, our retail banking products are competitive with those of other providers.

Government Regulation

As a payments processor to higher education institutions that takes payment instructions from institutions and their constituents, including students and employees, and gives them to our bank partner, we are directly or indirectly subject to a variety of federal and state laws and regulations. The following discussion does not purport to be a complete description of all of the laws and regulations that may affect us or all aspects of those laws and regulations. To the extent statutory or regulatory provisions are described in this discussion, the description is qualified in its entirety by reference to the particular statutory or regulatory provisions.

Our contracts with most of our higher education institutional clients and our bank partner require us to comply with applicable laws and regulations, including, where applicable, regulations promulgated by the United States Department of Education regarding the handling of student financial aid funds received by institutions on behalf of their students under Title IV of the Higher Education Act of 1965, or Title IV; the Family Educational Rights and Privacy Act of 1975, or FERPA; the Electronic Fund Transfer Act and Regulation E promulgated thereunder, or Regulation E; the USA PATRIOT Act and related anti-money laundering requirements; and certain federal rules regarding safeguarding personal information, including rules implementing the privacy provisions of the Gramm-Leach-Bliley Act of 1999, or GLBA.

Higher Education Regulations

Because of the services we provide to some institutions with regard to the handling of Title IV funds, the Department of Education may deem us to be a third-party servicer under the Title IV regulations. Those regulations require a third-party servicer annually to submit a compliance audit conducted by outside independent auditors that covers the servicer s Title IV activities. Although we do not believe that we should be deemed a third-party servicer, as a precaution in the event that we were in fact deemed to be a third-party servicer in the future, each year we submit a Compliance Attestation Examination of the Title IV Student Financial Assistance Programs audit to the Department of Education, which includes a report by an independent audit firm. In addition, the yearly audit submission to the

Department of Education provides comfort to certain of our higher education institutional clients that we would be in compliance with the third-party servicer regulations if they were deemed to apply to us. We also provide this audit report to clients upon request to help them fulfill their compliance audit obligations as Title IV participating institutions.

If we were deemed to be a third-party servicer, certain other Title IV regulations would apply to our business. These include, for example, regulations making a third-party servicer jointly and severally liable with its client institution for any liability to the Department of Education arising out of the servicer s violation of Title IV or its implementing regulations, which could subject us to material fines related to acts or omissions of entities beyond our control. The Department of Education is also empowered to limit, suspend or terminate the violating servicer s eligibility to act as a third-party servicer and to impose significant civil penalties on the violating servicer.

Our higher education institutional clients are subject to FERPA, which prohibits educational institutions that receive any federal funding from disclosing certain personally identifiable information of any student to third parties without the student s consent, subject to certain exceptions. Our higher education institutional clients disclose to us certain information concerning their students, including contact information, student identification numbers and the amount of students credit balances. We believe that our higher education institutional clients may disclose this information to us pursuant to one or more exceptions to FERPA disclosure prohibition.

Additionally, as we are indirectly subject to FERPA, we may not permit the transfer of any personally identifiable information to another party other than in a manner in which an educational institution may disclose it. While we believe that we have adequate policies and procedures in place to safeguard against the risk of disclosure of this information to third parties, a breach of this prohibition could result in a five-year suspension of our access to the related client s records. We may also be subject to similar state laws and regulations that restrict higher education institutions from disclosing certain personally identifiable information of students. For example, an Illinois law passed in 2009 prohibits certain public higher education institutions in Illinois from providing personally identifiable information of students to businesses that issue credit or debit cards.

Banking Regulations

The Bancorp Bank, or the Bank, our bank partner, is an insured depository institution, and funds held in each deposit account at our bank partner are insured by the FDIC up to applicable limits. As an insured depository institution, our bank partner is subject to comprehensive government regulation and, in the course of making its services available to our customers, we are required to assist the bank in complying with certain of its regulatory obligations. Among other laws and regulations, the anti-money laundering provisions of the USA PATRIOT Act require that customer identifying information be obtained and verified whenever a bank account is established. For example, because we facilitate the opening of deposit accounts at the Bank on behalf of our customers, we assist the Bank in collecting the basic customer identification information that is necessary to open an account. In addition, both we and the Bank are subject to the laws and regulations enforced by the Office of Foreign Assets Control, or OFAC, which prohibit U.S. persons from engaging in transactions with certain prohibited persons. As a service provider to an insured depository institution, we are required under federal law to agree to submit to examination by our bank partner s primary federal regulator, which is currently the FDIC. We also are subject to audit by our bank partner to ensure that we comply with our obligations to it appropriately. Failure to comply with our responsibilities properly could negatively affect our operations. Our bank partner is required under its agreement with us to, and we rely on our bank partner s ability to, comply with state and federal banking regulations.

The Bank provides demand deposit services for OneAccounts through a private label relationship. We provide processing services for these OneAccounts for the Bank. These services are subject to, among other things, the requirements of the Electronic Fund Transfer Act and the Federal Reserve Board s Regulation E, which govern automatic deposits to and withdrawals from deposit accounts and customers rights and liabilities arising from the use of ATMs, debit cards and other electronic banking services. Regulation E, among other things, requires initial disclosures of the terms and conditions of

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electronic fund transfers, dissemination of periodic statements to consumers for each monthly cycle in which an electronic fund transfer has occurred and prompt investigation and resolution of reported errors in electronic funds transfers. Regulation E also provides for limits on customer liability for transactions made with lost or stolen debit cards based upon the timeliness of the customer s notification of the loss or theft. In conjunction with the Bank, we promptly investigate and seek to resolve any reported errors related to the electronic banking services provided to our customers.

The Federal Reserve Board amended Regulation E to limit the ability of financial institutions, effective July 1, 2010, to assess an overdraft fee for paying ATM and one-time debit card transactions that overdraw a consumer s account, unless the consumer affirmatively consents, or opts in, to the institution s payment of overdrafts for these services. We and our banking partner adopted these changes, but we do not currently offer the opt in feature to our customer for ATM or one-time debit card transactions.

On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act, or the Act, was signed into law. The Act will increase the already substantial regulation and oversight of the financial services industry and imposes restrictions on the ability of firms within the industry, including us, to conduct business consistent with historical practices. For example, under the Act, a Consumer Financial Protection Bureau will be established to regulate any person engaged in a financial activity in connection with a consumer financial product or service, including those, such as us, that process financial services products and services. The new agency will have regulatory authority for many of the laws to which we and the Bank, are subject and may have direct supervisory authority over us. Additionally, the new agency will implement and oversee new regulations relating to consumer financial protection designed to prevent unfair, deceptive, and abusive practices in the offering of consumer financial products.

The Act also requires changes to be made to the manner in which merchants accept and process certain debit- and credit-card transactions. The Act, subject to certain exemptions, requires the Federal Reserve to impose limits on debit card interchange fees tied to the cost of processing the transaction, which may have the result of decreasing revenue to debit card issuers and processors. In December 2010, the Federal Reserve proposed a new Regulation II that, among other things, would limit interchange fees on debit card transactions to a maximum of 12 cents per transaction. If included in the final Regulation II, this maximum limit could significantly reduce interchange fees received by debit card issuers. Although these restrictions technically will apply only to debit card issuers with assets in excess of $10 billion, it is anticipated that smaller issuers, such as the Bank, may also be affected. Some federal, state, and local government-administered payment programs that use debit cards are exempt from this interchange fee restriction.

Additionally, the Act permits merchants to offer a discount or other incentive to encourage use of one form of payment over another, and it prohibits restrictions on merchants choice of payment processing networks. The Act allows merchants to set a minimum purchase threshold for credit card transactions provided such threshold does not exceed $10, and it permits institutions of higher education and federal agencies which constitute many of our clients to impose maximum dollar amounts for credit-card purchases.

Individual state legislatures are also reviewing interchange fees, and legislators in a number of states have proposed bills that purport to limit interchange fees or merchant discount rates or to prohibit their application to portions of a transaction.

Federal and state regulatory agencies also frequently propose and adopt changes to their regulations or change the manner in which existing regulations are applied. We cannot predict the substance or impact of pending or future legislation or regulation, or the application thereof, although enactment of the proposed legislation would affect how we and our bank partner operate and could significantly increase costs, impede the efficiency of internal business processes and limit our ability to pursue business opportunities in an efficient manner. See Part I, Item 1A. Risk Factors of this report.

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Privacy and Data Regulation

We are subject to laws and regulations relating to the collection, use, retention, security and transfer of personally identifiable information and data regarding our customers and their financial information. In addition, we are bound by our own privacy policies and practices concerning the collection, use and disclosure of user data, which are posted on certain of our websites.

In conjunction with the disbursement, payroll and tuition payment services we make available through our bank partner, it is necessary to collect certain information from our customers (such as bank account and routing numbers) to transmit to the bank. The bank uses this information to execute the funds transfers requested by our customers. These funds transfers are accomplished primarily by means of ACH networks and other wire transfer systems, such as FedWire. To the extent the data required by these electronic funds networks change, the information that we will be required to request from our clients may also change.

We are subject, either directly or by virtue of our contractual relationship with our bank partner, to the privacy and security standards of the GLBA privacy regulations, as well as certain state data protection laws and regulations. The GLBA privacy regulations require that we develop, implement and maintain a written comprehensive information security program prescribing safeguards that are appropriate to our size and complexity, the nature and scope of our activities and the sensitivity of any personally identifiable information we access for processing purposes or otherwise maintain. As a service provider of the Bank, we also are limited in our use and disclosure of the personal information we receive from the bank, which we may use and disclose only for the purposes for which it was provided to us, and consistent with the bank s own data privacy and security obligations. We also are subject to the standards set forth in guidance on data security issued by the Federal Financial Institution Examination Council, as well as the data security standards imposed by the card associations, including Visa, Inc., and MasterCard. In addition, we are subject to similar data security breach laws enacted by a number of states. Several other states are considering similar legislation.

New legislation and regulations in this area have been proposed, both at the federal and state level. Such measures, including pending federal legislation, would potentially impose additional obligations on us, including requiring that we provide notifications to consumers and government authorities in the event of a data breach or unauthorized access or disclosure, beyond what state law already requires. The interpretation of pending legislation and regulations, as well as some of the existing laws and regulations, is evolving and, therefore, these laws and regulations may be applied inconsistently. Under some interpretations, it is possible that our current data protection policies and practices may be deemed inconsistent with legal requirements, and breaches in the security of our technology systems and infrastructure could result in a violation of these laws and regulations.

Compliance

We monitor our compliance through an internal audit program. Our full-time internal auditor works with a third-party internal audit firm to conduct annual reviews to ensure compliance with the regulatory requirements described above. The costs of these audits and the costs of complying with the applicable regulatory requirements are significant. Increased regulatory requirements on our products and services, such as in connection with the matters described above, could materially increase our costs or reduce revenue.

Regulatory Inquiry

Because our technology services are provided in connection with the financial products of our bank partner, our activities are occasionally reviewed by regulatory agencies to ensure that we do not impermissibly engage in activities that require licensing at the state or federal level or that otherwise may be deemed to be in violation of law. In the ordinary course of business, we receive letters and inquiries concerning the nature of our business as it applies to state money transmitter licensing and regulations from different state regulatory agencies including but not limited to the State of Texas Department of Banking, the State of Washington Department of Financial Institutions and the State of Oregon Department of Consumer and Business Services. To date, we have cooperated with such inquiries by

explaining the nature of our business, which, to our knowledge, has satisfied the inquiring authorities. In 2007, the New York Attorney General launched an investigation into practices in the higher education industry involving certain of our higher education institutional clients. Pursuant to a subpoena, we have provided certain information about our clients and our business practices to the New York Attorney General. We most recently submitted information in November 2010. We cannot predict whether we will become subject to any formal investigation or other action by the New York Attorney General or any other state agencies.

Our operations and the operations of our bank partner are subject to the jurisdiction and examination of federal, state and local regulatory authorities, including the FDIC, which is our bank partner s primary federal regulator. Following a recently conducted compliance examination, the New York Regional Office of the FDIC notified us that it is prepared to recommend to the Director of FDIC Supervision that an enforcement action be taken against us for alleged violations of certain applicable laws and regulations principally relating to our compliance management system and policies and practices for past overdraft charging which we believe to have impacted persistently delinquent accounts, which is a small percentage of our total accounts, collections, and transaction error resolution. Any such enforcement action could result in an order to pay restitution and civil money penalties. We are in the process of responding to the FDIC s notification and we believe that we have voluntarily either remedied or taken steps to correct the alleged violations. For example, in connection with our review of the Overdraft Payment Programs and Consumer Protection Final Overdraft Payment Supervisory Guidance which requires modifications, if necessary, to be put in place prior to July 1, 2011, we reviewed our item processing procedures in December 2010 to ensure that transactions were not processed in a manner designed to maximize the cost to consumers. Any ultimate liability resulting from such an action we believe will not have a material adverse effect on our results of operations, financial position or cash flows, but there can be no assurances as to the outcome of this process. See Part 2, Item 1A. Risk Factors Reviews and enforcement actions by regulatory authorities under banking and consumer protection laws and regulations may result in changes to our business practices or may expose us to the risk of fines, restitution and litigation of this report.

Employees

As of December 31, 2010, we had approximately 450 employees. In addition, during periods of peak activity, we add temporary staff to supplement our customer service department. None of our employees is a member of any labor union or subject to any collective bargaining agreement and we have never experienced any business interruption as a result of any labor dispute.

Available Information

The Securities and Exchange Commission, or SEC, maintains a website that contains reports, proxy and information statements, and other information regarding issuers, including us, that file electronically with the SEC. The public can obtain any documents that we file with the SEC at http://www.sec.gov. We file annual reports, quarterly reports, proxy statements and other documents with the under the Securities Exchange Act of 1934, as amended, or the Exchange Act. The public may read and copy any materials that we file with the SEC at the SEC s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330.

We also make available free of charge through our website (http://ir.higherone.com) our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and, if applicable, amendments to those reports filed or furnished pursuant to the Exchange Act as soon as reasonably practicable after we electronically file such material with, or furnishes it to, the SEC. Information on our website is not incorporated into this report or any of our SEC filings and is not a part of them.

Item 1A. Risk Factors

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Our financial condition and results of operations are subject to various risks, uncertainties and other factors. These risks and uncertainties include, but are not limited to, the risk factors set forth below. The risks and uncertainties described in this report are not the only ones we face. Additional risks and uncertainties not presently known to us or that we currently believe are immaterial may also affect our business. If any of these known or unknown risks or uncertainties actually occurs, they could have a material adverse effect on our business, financial condition and results of operations.

Our operating results may suffer because of substantial and increasing competition in the industries in which we do business.

The market for our products and services is competitive, continually evolving and, in some cases, subject to rapid technological change. Our disbursement services compete against all forms of payment, including paper-based transactions (principally cash and checks), electronic transactions such as wire transfers and Automated Clearing House, or ACH, payments and other electronic forms of payment, including card-based payment systems. Many competitors, including Sallie Mae, TouchNet Information Systems, Inc., PNC Financial Services Goup, Inc. and Nelnet, Inc., provide payment software, products and services that compete with those we offer. In addition, our OneAccount and OneCard products and services, which we provide through our bank partner, also compete with banks active in the higher education market, including U.S. Bancorp and Wells Fargo & Company. Future competitors may begin to focus on higher education institutions in a manner similar to us.

Many of our competitors have substantially greater financial and other resources than we have, may in the future offer a wider range of products and services and may use advertising and marketing strategies that achieve broader brand recognition or acceptance. In addition, our competitors may develop new products, services or technologies that render our products, services or technologies obsolete or less marketable. If we cannot continue to compete effectively against our competitors, our business, financial condition and results of operations will be materially and adversely affected.

Reviews and enforcement actions by regulatory authorities under banking and consumer protection laws and regulations may result in changes to our business practices or may expose us to the risk of fines, restitution and litigation.

Our operations and the operations of our bank partner are subject to the jurisdiction and examination of federal, state and local regulatory authorities, including the FDIC, which is our bank partner s primary federal regulator. Our business practices, including the terms of our products, are approved by our banking partner and subject to both periodic and special reviews by such regulatory authorities, which can range from investigations into specific consumer complaints or concerns to broader inquiries into our practices generally. We and our bank partner are subject to ongoing and routine examination by the FDIC. If, as part of an examination or review, the regulatory authorities conclude that we are not complying with applicable laws or regulations, they could request or impose a wide range of remedies, including, but not limited to, requiring changes to the terms of our products (such as decreases in fees), the imposition of fines or penalties or the institution of enforcement proceedings or other similar actions against us alleging that our practices constitute unfair or deceptive acts or practices. As part of an enforcement action, the regulators can seek restitution for affected customers and impose civil money penalties. In addition, negative publicity relating to any specific inquiry or investigation or any related fine could adversely affect our stock price; our relationships with various industry participants; or our ability to attract new and retain existing clients, which could have a material adverse effect on our business, financial condition and results of operations.

Following a recently conducted compliance examination, the New York Regional Office of the FDIC notified us that it is prepared to recommend to the Director of FDIC Supervision that an enforcement action be taken against us for alleged violations of certain applicable laws and regulations principally relating to our compliance management system and policies and practices for past overdraft charging on persistently delinquent accounts, collections and transaction error resolution. Any such enforcement

action could result in an order to pay restitution and civil money penalties. We are in the process of responding to the FDIC s notification, but there can be no assurances as to the outcome of this process. An action instituted against us that results in significant changes to our practices, the imposition on us of fines or penalties, or an obligation for us to pay restitution or civil money penalties could have a material adverse effect on our business, financial condition and results of operations.

The fees that we generate through our relationships with higher education institutions and their campus communities are subject to competitive pressures and are subject to change, which may materially and adversely affect our revenue and profitability.

We generate revenue from, among other sources, the banking services fees charged to our OneAccount holders, interchange fees related to purchases made through our OneCard debit and ATM cards, which our bank partner charges and remits to us, convenience fees from processing tuition payments on behalf of students, fees charged to our higher education institution clients and service fees that we receive from our bank partner based on amounts deposited in OneAccounts and prevailing interest rates.

In an increasingly price-conscious and competitive market, it is possible that to maintain our competitive position with higher education institutions, we may have to decrease the fees we charge institutions for our services. Similarly, in order to maintain our competitive position with our OneAccount holders, we may need to work with our bank partner to reduce banking services fees charged to our OneAccount holders.

MasterCard could reduce the interchange rates, which it unilaterally sets and adjusts from time to time, and upon which our interchange revenue is dependent. In addition, our OneAccount holders may modify their spending habits and increase their use of ACH relative to their use of OneCards, as ACH payments are generally free, which could reduce the interchange fees remitted to us. Students may also become less willing to pay convenience fees when using our payment transaction services. If our fees are reduced as described above, our business, results of operations and prospects for future growth could be materially and adversely affected.

Fees for financial services are subject to increasingly intense legislative and regulatory scrutiny, which could have a material adverse effect on our business, financial condition, results of operations and prospects for future growth.

In 2010, 2009 and 2008, approximately 78%, 88% and 85% of our revenue was generated from interchange fees, ATM fees, non-sufficient funds fees, other banking services fees and convenience fees. These fees, as well as the financial services industry in general, have undergone or may undergo substantial changes in the near future. These changes could have a material adverse effect on our business, financial condition, results of operations and prospects for future growth.

Effective July 1, 2010, the Federal Reserve Board amended Regulation E to limit the ability of financial institutions to assess an overdraft fee for paying ATM and one-time debit card transactions that overdraw a consumer s account, unless the consumer affirmatively consents, or opts in, to the institution s payment of overdrafts for these services. In the absence of such a consent, a financial institution may not assess an overdraft fee on a consumer for an ATM or one-time debit card transaction.

On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act, or the Act, was signed into law. The Act will increase the already substantial regulation and oversight of the financial services industry and imposes restrictions on the ability of firms within the industry, including us, to conduct business consistent with historical practices. For example, under the Act, a Consumer Financial Protection Bureau will be established to regulate any person engaged in a financial activity in connection with a consumer financial product or service, including those, such as us, that process financial services products and services. The new agency will have regulatory authority for many of the

laws to which we and our partner bank, The Bancorp Bank, are subject and may have direct supervisory authority over us, and it will implement and oversee new regulations relating to consumer financial protection designed to prevent unfair, deceptive, and abusive practices in the offering of consumer financial products.

The Act also requires changes to be made to the manner in which merchants accept and process certain debit- and credit-card transactions. The Act, subject to certain exemptions, requires the Federal Reserve to impose limits on debit card interchange fees tied to the cost of processing the transaction, which may have the result of decreasing revenue to debit card issuers and processors. In December 2010, the Federal Reserve proposed a new Regulation II that, among other things, would limit interchange fees on debit card transactions to a maximum of 12 cents per transaction. If included in the final Regulation II, this maximum limit could significantly reduce interchange fees received by debit card issuers. Although these restrictions technically will apply only to debit card issuers with assets in excess of $10 billion, it is anticipated that smaller issuers, such as The Bancorp Bank, may also be impacted. Some federal, state, and local government-administered payment programs that use debit cards are exempt from this interchange fee restriction. Additionally, the Act permits merchants to offer a discount or other incentive to encourage use of one form of payment over another, and it prohibits restrictions on merchants choice of payment processing networks. The Act allows merchants to set minimum purchase thresholds for credit card transactions, provided such thresholds do not exceed $10, and it permits institutions of higher education and federal agencies which constitute many of our clients to impose maximum dollar amounts for credit-card purchases. Individual state legislatures are also reviewing interchange fees, and legislators in a number of states have proposed bills that purport to limit interchange fees or merchant discount rates or to prohibit their application to portions of a transaction.

Many of the provisions of the Act will not become effective until a year or more following its enactment and after the adoption and effectiveness of implementing regulations. The scope and impact of many of the Act s provisions, moreover, will be determined through the rule making process. As a result, we cannot predict the ultimate impact of the Act on us or The Bancorp Bank at this time, nor can we predict the impact or substance of other future legislation or regulation. However, we believe that the Act, other recent changes in regulation, including the Regulation E changes summarized above, and legislation under consideration by the states could affect how we and our bank partner operate by significantly reducing the interchange fees, ATM fees, non-sufficient fund fees, other banking services fees and convenience fees charged in respect of our services and that drive our financial results. These regulatory and legislative changes could also increase our costs, impede the efficiency of our internal business processes or limit our ability to pursue business opportunities in an efficient manner. The occurrence of any of these risks could materially and adversely affect our business, financial condition and results of operations.

We rely on our bank partner for certain banking services, and a change in relationship with our bank partner or its failure to comply with certain banking regulations could materially and adversely affect our business.

As the provider of FDIC-insured depository services for all of our OneAccounts, as well as other banking functions, such as supplying cash for our ATM machines, The Bancorp Bank, our bank partner, provides third-party services that are critical to our student-oriented banking services. If any material adverse event were to affect The Bancorp Bank, including, but not limited to, a significant decline in its financial condition, a decline in the quality of its service, loss of deposits, its inability to comply with applicable banking and financial service regulatory requirements, systems failure or its inability to pay us fees, our business, financial condition and results of operations could be materially and adversely affected. If we were required to change banking partners, we could not accurately predict the success of such change or that the terms of our agreement with a new banking partner would be as favorable to us, especially in light of the recent consolidation in the banking industry, which has rendered the market for FDIC-insured retail banking services less competitive.

The length and unpredictability of the sales cycle for signing potential higher education institution clients could delay new sales of our products and services, which could materially and adversely

affect our business, financial condition and results of operations.

The sales cycle between our initial contact with a potential higher education institution client and the signing of a contract with that client can be lengthy. As a result of this lengthy sales cycle, our ability to forecast accurately the timing of revenues associated with new sales is limited. Our sales cycle varies widely due to significant uncertainties, over which we have little or no control, including:

- the individual decision-making processes of each higher education institution client, which typically include extensive and lengthy evaluations and require us to spend substantial time, effort and money educating each client about the value of our products and services;
- the budgetary constraints and priorities and budget cycle of each higher education institution client; and
- the reluctance of higher education staff to change or modify existing processes and procedures.

In addition, there is no guarantee that a potential client will sign a contract with us even after we spend substantial time, effort and money on the potential client. A delay in our ability or a failure to enter into new contracts with potential higher education institution clients could materially and adversely affect our business, financial condition and results of operations.

We depend on our relationship with higher education institutions and, in turn, student usage of our products and services for future growth of our business.

Our future growth depends, in part, on our ability to enter into agreements with higher education institutions. While we have experienced significant growth since 2002 in the number of our higher education institution clients, our contracts with these clients can generally be terminated at will and, therefore, there can be no assurance that we will be able to maintain these clients. We may also be unable to maintain our agreements with these clients on terms and conditions acceptable to us. In addition, we may not be able to continue to establish new relationships with higher education institution clients at our historical growth rate or at all. The termination of our current client contracts or our inability to continue to attract new clients could have a material adverse effect on our business, financial condition and results of operations.

Not only are establishing new client relationships and maintaining current ones critical to our business, but they are also essential components of our strategy for maximizing student usage of our products and services and attracting new student customers. A reduction in enrollment, a failure to attract and maintain student customers, as well as any future demographic trends that reduce the number of higher education students could materially and adversely affect our capability for both revenue and cash generation and, as a result, could have a material adverse effect on our business, financial condition and results of operations.

Global economic and other conditions may adversely affect trends in consumer spending, which could materially and adversely affect our business, financial condition and results of operations.

A decrease in consumer confidence due to the weakening of the global economy may cause decreased spending among our student customers and may decrease the use of our OneAccount and OneCard products and services. Increases in college tuition alongside stagnation or reduction in available financial aid may also restrict spending among college students and the size of disbursements, reducing the use of our OneAccount and OneCard products and services and demand for our disbursement services, which could materially and adversely affect our business, financial condition and results of operations.

Failure to manage future growth effectively could have a material adverse effect on our business, financial condition and results of operations.

The continued rapid expansion and development of our business may place a significant strain

upon our management and administrative, operational and financial infrastructure. As of December 31, 2010, we had approximately 1.6 million OneAccounts, representing growth of 61% from December 31, 2009. In 2010, our total revenue, adjusted EBITDA, adjusted net income and net income were approximately $145.0 million, $59.5 million, $34.4 million and $25.1 million, respectively, which represents three-year compounded annual growth rates over 2007 of approximately 73%, 121%, 142% and 122%, respectively. See Part II, Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations of this report for definitions of adjusted EBITDA and adjusted net income and reconciliations to net income. Our growth strategy contemplates further increasing the number of our higher education institution clients and student banking customers, however, the rate at which we have been able to establish relationships with our customers in the past may not be indicative of the rate at which we will be able to establish additional customer relationships in the future.

Our success will depend in part upon the ability of our executive officers to manage growth effectively. Our ability to grow also depends upon our ability to successfully hire, train, supervise, and manage new employees, obtain financing for our capital needs, expand our systems effectively, control increasing costs, allocate our human resources optimally, maintain clear lines of communication between our operational functions and our finance and accounting functions, and manage the pressures on our management and administrative, operational and financial infrastructure. There can be no assurance that we will be able to accurately anticipate and respond to the changing demands we will face as we continue to expand our operations or that we will be able to manage growth effectively or to achieve further growth at all. Similarly, there can be no assurance that we will be able to effectively control the increasing costs and manage the additional demands placed on our finance and accounting staff and on our financial, accounting and information systems caused by our need to comply with public company requirements, such as those relating to disclosure controls and procedures and internal control over financial reporting. If our business does not continue to grow or if we fail to effectively manage any future growth or the increased costs and administrative burdens of being a public company, our business, financial condition and results of operations could be materially and adversely affected.

Our business and future success may suffer if we are unable to cross-sell our products and services.

A significant component of our growth strategy is dependent on our ability to cross-sell products and services to new and existing customers. In particular, our growth strategy depends on our ability to successfully cross-sell our disbursement services to our payment services clients and our payment services to our disbursement services clients. We may not be successful in cross-selling our products and services because our customers may find our additional products and services unnecessary or unattractive. Our failure to sell additional products and services to new and existing customers could have a material adverse effect on our prospects, business, financial condition and results of operations.

We depend on our founders and other key members of executive management and the loss of their services could have a material adverse effect on our business.

We substantially depend on the efforts, skill and reputations of our founders and senior management team including: Dean Hatton (President and CEO), Mark Volchek (Founder and CFO), Miles Lasater (Founder and COO), Casey McGuane (Chief Service Officer) and Robert Reach (Chief Sales Officer). We do not currently maintain key person life insurance policies with respect to our executive officers. None of our executive officers have entered into employment agreements with us, leaving them free to terminate their involvement with us at any time and/or to pursue other opportunities. The loss of any of our executive officers or founders could have a material adverse effect on our ability to manage our company, growth prospects, business financial condition and results of operations.

We have no operating history in rehabilitation and development activities and these activities are inherently risky and could adversely impact our business and strain management resources.

We are actively involved in a project to rehabilitate and develop two existing commercial buildings

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located in New Haven, Connecticut, which we expect will become our new corporate headquarters at the completion of the project. We do not have any prior operating history in property rehabilitation and development and therefore uncertainties and unknown future challenges that may arise in connection with these activities could divert management s attention from our core business and strain management s resources.

In addition, rehabilitation and development projects entail the following considerable risks:

- cost overruns including construction costs that may exceed our original estimates;
- unforeseen quality or engineering problems;
- construction delays;
- unanticipated financing costs;
- work stoppages and higher-than-estimated labor costs;
- weather interference;
- costs for the removal or remediation of hazardous or toxic substances present at, on, under or in or released from the project site; and
- delays with respect to obtaining or the inability to obtain necessary zoning, occupancy, land use and other governmental permits, and/or changes in zoning and land use laws.

If any of these problems occur, our plans to move into the facility may be delayed and the overall project costs may significantly exceed the costs that were estimated when the project was originally undertaken, which could have a material adverse effect on our business, financial condition and results of operations.

We may not be able to meet all of the criteria to obtain and retain various subsidies, grants and credits we expect to receive in connection with our rehabilitation and development project.

We expect to receive various subsidies, grants and credits from different state and federal agencies and private entities that will offset our investment in the rehabilitation project. Many of these programs have criteria that we must meet in order to receive the subsidies, grants and credits and also criteria that we must meet on an ongoing basis in order to prevent forfeiture of the subsidies, grants and credits, and in some cases the imposition of a penalty. If we are not able to meet either the initial or continuing criteria, we may forfeit some or all of the incentives which we are eligible for.

We are subject to substantial federal and state governmental regulation that could change and thus force us to make modifications to our business. Compliance with the various complex laws and regulations is costly and time consuming, and failure to comply could have a material adverse effect on our business. Additionally, increased regulatory requirements on our services may increase our costs, which could materially and adversely affect our business, financial condition and results of operations.

As a payments processor to higher education institutions that takes payment instructions from institutions and their constituents, including students and employees, and gives them to our bank partner, we are directly or indirectly subject to a variety of federal and state laws and regulations. Our contracts with most of our higher education institution clients and our bank partner require us to comply with applicable laws and regulations, including, where applicable:

Title IV;

FERPA;

the Electronic Fund Transfer Act and Regulation E;

the USA PATRIOT Act and related anti-money laundering requirements; and

certain federal rules regarding safeguarding personal information, including rules implementing the privacy provisions of GLBA.

Higher Education Regulations

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Third-Party Servicer. Because of the services we provide to some institutions with regard to the handling of Title IV funds, the Department of Education may deem us to be a third-party servicer under the Title IV regulations. Those regulations require a third-party servicer annually to submit a compliance audit conducted by outside independent auditors that covers the servicer s Title IV activities. Although we do not believe we should be deemed a third-party servicer, each year we submit a Compliance Attestation Examination of the Title IV Student Financial Assistance Programs audit to the Department of Education, which includes a report by an independent audit firm. We also provide this audit report to clients upon request to help them fulfill their compliance audit obligations as Title IV participating institutions.

If we were deemed to be a third-party servicer, certain other Title IV regulations would apply to our business. These include, for example, regulations making a third-party servicer jointly and severally liable with its client institution for any liability to the Department of Education arising out of the servicer s violation of Title IV or its implementing regulations, which could subject us to material fines related to acts or omissions of entities beyond our control. The Department of Education is also empowered to limit, suspend or terminate the violating servicer s eligibility to act as a third-party servicer and to impose significant civil penalties on the violating servicer. In the event the Department of Education concluded that we were a third-party servicer, had violated Title IV or its implementing regulations and should be subject to one or more of these sanctions, our business and results of operations could be materially and adversely affected. There is limited enforcement and interpretive history of Title IV regulations relevant to this risk factor.

FERPA. Our higher education institution clients are subject to FERPA, which prohibits educational institutions that receive any federal funding from disclosing certain personally identifiable information of any student to third parties without the student s consent, subject to certain exceptions. Our higher education institution clients disclose to us certain information concerning their students, including contact information, student identification numbers and the amount of students credit balances. We believe that our higher education institution clients may disclose this information to us pursuant to one or more exceptions to FERPA disclosure prohibition. However, if we do not fall into one of these exceptions or if future changes to legislation or regulations required student consent before our higher education institution clients could disclose this information to us, a sizeable number of students may cease using our products and services, which could materially and adversely affect our business, financial condition and results of operations.

Additionally, as we are indirectly subject to FERPA, we may not permit the transfer of any personally identifiable information to another party other than in a manner in which a higher education institution may disclose it. In the event that we re-disclose student information in violation of this requirement, FERPA requires our clients to suspend our access to any such information for a period of five years. Any such suspension could have a material adverse effect on our business, financial condition or results of operations.

State Laws. We may also be subject to similar state laws and regulations that restrict higher education institutions from disclosing certain personally identifiable information of students. For example, an Illinois law passed in 2009 prohibits certain public higher education institutions in Illinois from providing personally identifiable information of students to businesses that issue credit or debit cards. State attorneys generals and other enforcement agencies may monitor our compliance with state and federal laws and regulations pertaining to higher education and banking and conduct investigations of our business that are time consuming and expensive and could result in fines and penalties that have a material adverse effect on our business, financial condition and results of operations.

Regulation of OneAccounts

Anti-Money Laundering; USA PATRIOT ACT; OFAC. The Bancorp Bank, our bank partner, is an insured depository institution and funds held at our bank partner are insured by the FDIC up to applicable limits. As an insured depository institution, our bank partner is subject to comprehensive government

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regulation and, in the course of making its services available to our customers, we are required to assist the Bank in complying with certain of its regulatory obligations. In particular, the anti-money laundering provisions of the USA PATRIOT Act require that customer identifying information be obtained and verified whenever a bank account is established. For example, because we facilitate the opening of deposit accounts at the Bank on behalf of our customers, we assist the bank in collecting the basic customer identification information that is necessary to open an account. In addition, both we and the Bank are subject to the laws and regulations enforced by the OFAC, which prohibit U.S. persons from engaging in transactions with certain prohibited persons. Our failure to comply with any of these laws or rights could materially and adversely affect or business, financial credit and results of operations.

Compliance; Audit. As a service provider to an insured depository institution, we are required under federal law to agree to submit to examination by our bank partner s primary federal regulator, which is currently the FDIC. We also are subject to audit by our bank partner to ensure that we comply with our obligations to it appropriately. Failure to comply with our responsibilities properly could negatively affect our operations. Our bank partner is required under its agreement with us to, and we rely on our bank partner s ability to, comply with state and federal banking regulations. The failure of our bank partner to maintain regulatory compliance could result in significant disruptions to our business and have a material adverse effect on our business, financial condition and results of operations.

Electronic Fund Transfer Act; Regulation E. The Bancorp Bank provides demand deposit services for OneAccounts through a private label relationship. We provide processing services for these OneAccounts for the Bank. These services are subject to, among other things, the requirements of the Electronic Fund Transfer Act and the Federal Reserve Board s Regulation E, which govern automatic deposits to and withdrawals from deposit accounts and customers rights and liabilities arising from the use of ATMs, debit cards and other electronic banking services. We may assist our bank partner with fulfilling its compliance obligations pursuant to these requirements. See Part I, Item 1A. Risk Factors Fees for financial services are subject to increasingly intense legislative and regulatory scrutiny, which could have a material adverse effect on our business, financial condition, results of operations and prospects for future growth , of this report. Failure to comply with applicable regulations could materially and adversely affect our business, financial condition and results of operations.

Money Transmitter Regulations. Because our technology services are provided in connection with the financial products of our bank partner, our activities are occasionally reviewed by regulatory agencies to ensure that we do not impermissibly engage in activities that require licensing at the state or federal level. In the ordinary course of business, we receive letters and inquiries concerning the nature of our business as it applies to state money transmitter licensing and regulations from different state regulatory agencies. If a state agency were to conclude that we are required to be licensed as a money transmitter, we may need to undergo a costly licensing process in that state, and failure to comply could be a violation of state and potentially federal law.

Privacy and Data Regulation

We are subject to laws and regulations relating to the collection, use, retention, security and transfer of personally identifiable information and data regarding our customers and their financial information. In addition, we are bound by our own privacy policies and practices concerning the collection, use and disclosure of user data, which are posted on certain of our websites.

In conjunction with the disbursement, payroll and tuition payment services we make available through our bank partner, it is necessary to collect certain information from our customers (such as bank account and routing numbers) to transmit to the bank. The bank uses this information to execute the funds transfers requested by our customers, which are effected primarily by means of ACH networks and other wire transfer systems, such as FedWire. To the extent the data required by these electronic funds networks change, the information that we will be required to request from our clients may also change.

We are subject, either directly or by virtue of our contractual relationship with our bank partner, to the privacy and security standards of the GLBA privacy regulations, as well as certain state data protection laws and regulations. The GLBA privacy regulations require that we develop, implement and maintain a written comprehensive information security program prescribing safeguards that are appropriate to our size and complexity, the nature and scope of our activities and the sensitivity of any personally identifiable information we access for processing purposes or otherwise maintain. As a service provider of the Bank, we also are limited in our use and disclosure of the personal information we receive from the Bank, which we may use and disclose only for the purposes for which it was provided to us and consistent with the bank s own data privacy and security obligations. We also are subject to the standards set forth in guidance on data security issued by the Federal Financial Institution Examination Council, as well as the data security standards imposed by the card associations, including Visa, Inc., and MasterCard. In addition, we are subject to similar data security breach laws enacted by a number of states. Several other states are considering similar legislation.

Any failure or perceived failure by us to comply with any legal or regulatory requirements or orders or other federal or state privacy or consumer protection-related laws and regulations, or with our own privacy policies, could result in fines, sanctions, litigation, negative publicity, limitation of our ability to conduct our business and injury to our reputation, any of which could materially and adversely affect our business, financial condition and results of operations.

New legislation and regulations in this area have been proposed, both at the federal and state level. Such measures, including pending Federal legislation, would potentially impose additional obligations on us, including requiring that we provide notifications to consumers and government authorities in the event of a data breach or unauthorized access or disclosure, beyond what state law already requires. The interpretation of pending legislation and regulations, as well as some of the existing laws and regulations, is evolving and, therefore, these laws and regulations may be applied inconsistently. Under some interpretations, it is possible that our current data protection policies and practices may be deemed inconsistent with legal requirements, and breaches in the security of our technology systems and infrastructure could result in a violation of these laws and regulations. These laws and regulations could cause us to incur substantial costs or require us to change our business practices in a manner materially adverse to our business.

Compliance

We monitor our compliance through an internal audit program. Our full-time internal auditor works with a third-party internal audit firm to conduct annual reviews to ensure compliance with the regulatory requirements described above. The costs of these audits and the costs of complying with the applicable regulatory requirements are significant. Increased regulatory requirements on our products and services, such as in connection with the matters described above, could materially increase our costs or reduce revenue.

It is impossible to determine the extent of the impact of any new laws, regulations or initiatives that may be proposed, or whether any of the proposals will become law. The imposition of any new laws or regulations could make compliance more difficult and expensive and affect the manner in which we conduct business. In addition, many of these laws and regulations are evolving, unclear and inconsistent across various jurisdictions. If we were deemed to be in violation of any laws or regulations that are currently in place or that may be promulgated in the future, including but not limited to those described above, we could be exposed to financial liability and adverse publicity or forced to change our business practices or stop offering some of our products and services. We also could face significant legal fees, delays in extending our product and services offerings, and damage to our reputation that could harm our business and reduce demand for our products and services. Even if we are not required to change our business practices, we could be required to obtain licenses or regulatory approvals that could cause us to incur substantial costs and delays.

The convenience fees that we charge in connection with payment transactions are subject to

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change.

Most credit and debit card associations and networks permit us to charge convenience fees to students, parents or other payers who make online payments to our higher education institution clients through the SmartPay feature of our ePayment product using a credit or debit card. In 2010 and 2009, these convenience fees accounted for substantially all of our payment transaction revenue, which is a trend we expect to continue going forward. While the majority of credit and debit card associations and networks routinely permit merchants and other third parties to charge these fees, it is not a ubiquitous practice in the payment industry. If these credit and debit card associations and networks change their policies in permitting merchants and other third-parties to charge these fees or otherwise restrict our ability to do so, our business, financial condition and results of operations could be materially and adversely affected.

There are risks associated with charging convenience fees.

Through our SmartPay service, which we acquired in connection with our acquisition of IDC, which we renamed Higher One Payments, Inc., in 2009, some of our higher education institution clients charge convenience fees to students, parents or other payers who make online payments using a credit or debit card. In light of the ongoing legislative efforts at financial regulatory reform, we examined the laws and regulations related to convenience fees. We found that these laws and regulations vary from state to state and certain states, including California, Florida, Massachusetts, New York and Texas, have laws that to varying degrees prohibit the imposition of a surcharge on a credit or debit cardholder who elects to use a credit or debit card in lieu of payment by cash, check or other means. The penalties for violating these laws vary from state to state and include, in certain circumstances, fines that could be significant.

We are not aware of any enforcement or civil action against a higher education institution or a third party service provider for charging convenience fees. We have nevertheless worked with our higher education institution clients to ensure that we can continue to provide the services they demand, while ensuring we are in compliance with these laws and regulations prospectively. The affected revenues to us are not significant. However, if one or more states or other parties initiate an action against us, we could be subject to a claim for significant fines or damages. Moreover, the institution of any such action could disrupt our operations or result in negative publicity, which could diminish our ability to attract new and retain existing clients, and could materially and adversely affect our prospects, business, financial condition and results of operations.

Our business depends on the current government financial aid regime that relies on the outsourcing of financial aid disbursements through higher education institutions.

In general, the U.S. federal government distributes financial aid to students through higher education institutions as intermediaries. Following the receipt of financial aid funds and the payment of tuition and other expenses, higher education institutions have typically processed refund disbursements to students by preparing and distributing paper checks. Our OneDisburse® service provides our higher education institution clients an electronic system for improving the administrative efficiency of this refund disbursement process. If the government, through legislation or regulatory action, restructures the existing financial aid regime in such a way that reduces or eliminates the intermediary role played by financial institutions serving higher education institutions or limits or regulates the role played by service providers such as us, our business, results of operations and prospects for future growth could be materially and adversely affected.

A change in the availability of financial aid, as well as budget constraints, could materially and adversely affect our financial performance by reducing demand for our services.

The higher education industry depends heavily upon the ability of students to obtain financial aid. As part of our contracts with our higher education institution clients that use OneDisburse®, students

financial aid and other refunds are sent to us for disbursement. The fees that we charge most of our OneDisburse® higher education institution clients are based on the number of financial aid disbursements that we make to students. In addition, our relationships with OneDisburse® higher education institution clients provide us with a market for OneAccounts, from which we derive a significant proportion of our revenues. Consequently, a change in the availability of financial aid that restricted client use of our OneDisburse® product or otherwise limited our ability to attract new higher education institution clients could materially and adversely affect our financial performance. Future legislative and executive branch efforts to reduce the U.S. federal budget deficit or worsening economic conditions may require the government to severely curtail its financial aid spending, which could materially and adversely affect our business, financial condition and results of operations.

Termination of, or changes to, the MasterCard association registration could materially and adversely affect our business, financial condition and results of operations.

We and our bank partner, which issues our OneCards, are subject to MasterCard association rules that could subject us to a variety of fines or penalties that may be levied by MasterCard for acts or omissions by us or businesses that work with us. The termination of the card association registration held by us or our bank partner or any changes in card association or other network rules or standards, including interpretation and implementation of existing rules or standards, that increase the cost of doing business or limit our ability to provide our products and services could materially and adversely affect our business, financial condition and results of operations.

Intellectual property infringement claims against us could be costly and time-consuming to defend and if we are unsuccessful in our defense could have a material adverse effect on our business, financial condition and results of operations.

Third parties may assert, including by means of counter-claims against us as a result of the assertion of our intellectual property rights, that our products, services or technology, or the operation of our business, violate their intellectual property rights. As the number of competitors in our industry increases and the functionality of technology offerings further overlap, such claims and counter-claims could become more common. We cannot be certain that we do not or will not infringe third parties intellectual property rights.

Any intellectual property claim against us, regardless of its merit, could result in significant liabilities to our business. Depending on the nature of such claim, our business may be disrupted, our management s attention and other company resources may be diverted and we may be required to redesign our products and services or to enter into royalty or licensing agreements in order to obtain the rights to use necessary technologies, which may not be available on terms acceptable to us, if at all. If we cannot redesign our products and services or license necessary technologies, we may be subject to the risk of injunctive relief and/or significant damage awards, which are complex, subjective and hard to predict, and subsequently we may not be able to offer or sell a particular product or service, or a family of products or services.

Any intellectual property claim against us could be expensive and time consuming to defend. Insurance may not cover or be insufficient for such claim, or may not be available on terms acceptable to us. A claim brought against us that is uninsured or underinsured could result in unanticipated costs, thereby having a material adverse effect on our business, financial condition and results of operations. Even if we have an indemnification arrangement with a third party to indemnify us against an intellectual property claim, such indemnifying party may be unable or fail to uphold its contractual obligations to us. If any infringement or other intellectual property claim that is brought against us is successful, our business, operating results and financial condition could be materially and adversely affected.

Current and future litigation against us could be costly and time-consuming to defend.

We are from time to time subject to legal proceedings and claims that arise in the ordinary course of business. Litigation may result in substantial costs and may divert management s attention and resources, which may materially and adversely affect our business, financial condition and results of operations. In addition, legal claims that have not yet been asserted against us may be asserted in the future. Insurance may not cover such claims, be sufficient for one or more such claims, or continue to be available on terms acceptable to us.

In particular, a third party may assert that our technology violates its intellectual property rights. As the number of products in our industry increases and the functionality of these products further overlap, infringement claims could become more common. Any claims, regardless of their merit, could be expensive and time consuming to defend, require us to redesign our products, divert management s attention and other company resources and require us to enter into royalty or licensing agreements in order to obtain the right to use necessary technologies, which may not be available on terms acceptable to us, if at all. A claim brought against us that is uninsured or underinsured could result in unanticipated costs, thereby reducing our operating results and leading analysts or potential investors to reduce their expectations of our performance resulting in a reduction in the trading price of our stock. See Part I, Item 3. Legal Proceedings, of this report.

General economic conditions may adversely affect our ability to raise capital in the future.

We may need or seek additional financing in the future to refinance our existing credit facility, fund our operations, fund acquisitions, develop additional products and services or implement other projects. As of December 31, 2010, Higher One, Inc. had no borrowings outstanding under its senior secured revolving credit facility. Given the state of the current credit environment resulting from, among other things, the general weakening of the global economy, it may be difficult to refinance our credit facility or obtain any additional financing on acceptable terms, which could have an adverse effect on our business, financial condition and results of operations. In addition, if, as a result of the current conditions in the credit markets, the lenders under our current credit agreement or any other lender under any future credit agreement is unable to fund borrowings under that agreement, our liquidity could be adversely affected.

The terms of our credit agreement may restrict our current and future operations, which would adversely affect our ability to respond to changes in our business and to manage our operations.

Our credit agreement contains, and any future indebtedness of ours would likely contain, a number of restrictive covenants that impose significant operating and financial restrictions on us, including restrictions on our ability to, among other things:

- create liens;
- make investments and acquisitions;
- incur additional debt;
- transfer all or substantially all of our assets or enter into merger or consolidation transactions;
- dispose of assets;
- pay dividends or make any other distributions with respect to our stock;
- issue stock, warrants, options or other rights to purchase stock or securities convertible into or exchangeable for shares of stock;

- engage in any material line of business substantially different from the lines of business we currently conduct or any business substantially related or incidental thereto; and

- enter into transactions with affiliates.

Our ability to comply with these covenants may be affected by events beyond our control, and any material deviations from our forecasts could require us to seek waivers or amendments of covenants or alternative sources of funding. We cannot assure you that such waivers, amendments or alternative

sources of funding could be obtained, or if obtained, would be on terms acceptable to us.

Our credit agreement also requires us to maintain certain liquidity levels and satisfy certain financial ratios, including a maximum total leverage ratio and a minimum interest coverage ratio. A failure by us to comply with the covenants contained in our credit agreement could result in an event of default which could adversely affect our ability to respond to changes in our business and manage our operations. An event of default would also occur under our credit agreement if we undergo a change of control or if we experience a material adverse change in our operations, condition or prospects. In the event of any default under our credit agreement, the lender could elect to declare all amounts outstanding to be due and payable and require us to apply all of our available cash to repay these amounts. The acceleration of indebtedness under our credit agreement could have a material adverse effect on our business, financial condition and results of operations.

We outsource critical operations, which exposes us to risks related to our third-party vendors.

We have entered into contracts with third-party vendors to provide critical services, technology and software in our operations. These outsourcing partners include: Fiserv, which provides back-end account and transaction data processing for OneAccounts and OneCards; MasterCard, which provides the payment network for our OneCards, as well as for certain other transactions; Comerica and Global Payments, which provide transaction processing and banking services for payment processing related to the SmartPay feature of our ePayment service; and Terremark and Neospire, which provide web and application hosting services in secure data centers.

Accordingly, we depend, in part, on the services, technology and software of these and other third-party service providers. In the event that these service providers fail to maintain adequate levels of support, do not provide high quality service, discontinue their lines of business, terminate our contractual arrangements or cease or reduce operations, we may be required to pursue new third-party relationships, which could materially disrupt our operations and our ability to provide our products and services, and could divert management s time and resources. Replacement technology or services provided by replacement third-party vendors could be more expensive than those we have currently, while the process of transitioning services and data from one provider to another can be complicated and time consuming. If we are unable to complete a transition to a new provider on a timely basis, or at all, we could be forced to temporarily or permanently discontinue certain services, which could disrupt services to our customers and materially and adversely affect our business, financial condition and results of operations. We may also be unable to establish comparable new third-party relationships on as favorable terms or at all, which could materially and adversely affect our business, financial condition and results of operations.

Breaches of security measures, unauthorized access to or disclosure of data relating to our clients, fraudulent activity, and infrastructure failures could materially and adversely affect our reputation or harm our business.

Our higher education institution clients and student OneAccount holders disclose to us certain personally identifiable information, including student contact information, identification numbers and the amount of credit balances, which they expect we will maintain in confidence. It is possible that hackers, customers or employees acting unlawfully or contrary to our policies, or other individuals, could improperly access our or our vendors systems and obtain or disclose data about our customers. Further, because customer data may also be collected, stored, or processed by third party vendors, it is possible that these vendors could intentionally, negligently or otherwise disclose data about our clients or customers.

We rely to a large extent upon sophisticated information technology systems, databases, and infrastructure, and take reasonable steps to protect them. However, due to their size, complexity, content and integration with or reliance on third party systems they are potentially vulnerable to breakdown, malicious intrusion, natural disaster and random attack, all of which pose a risk that sensitive data may be

exposed to unauthorized persons or to the public.

A breach of our information systems could lead to fraudulent activity, including with respect to our OneCards, such as identity theft, losses on the part of our banking customers, additional security costs, negative publicity and damage to our reputation and brand. In addition, our customers could be subject to scams that may result in the release of sufficient information concerning themselves or their accounts to allow others unauthorized access to their accounts or our systems (e.g., phishing and smishing). Claims for compensatory or other damages may be brought against us as a result of a breach of our systems or fraudulent activity. If we are unsuccessful in defending against any resulting claims against us, we may be forced to pay damages, which could materially and adversely affect our financial condition and results of operations.

In addition, a significant incident of fraud or an increase in fraud levels generally involving our products, such as our OneCards, could result in reputational damage to us, which could reduce the use of our products and services. Such incidents of fraud could also lead to regulatory intervention, which could increase our compliance costs. See Part I, Item 1A. Risk Factors We are subject to substantial federal and state governmental regulation that could change and thus force us to make modifications to our business. Compliance with the various complex laws and regulations is costly and time consuming, and failure to comply could have a material adverse effect on our business. Additionally, increased regulatory requirements on our services may increase our costs, which could materially and adversely affect our business, financial condition and results of operations of this report. Accordingly, account data breaches and related fraudulent activity could have a material adverse effect on our future growth prospects, business, financial condition and results of operations.

A disruption to our systems or infrastructure could damage our reputation, expose us to legal liability, cause us to lose customers and revenue, result in the unintentional disclosure of confidential information or require us to expend significant efforts and resources or incur significant expense to eliminate these problems and address related data and security concerns. The harm to our business could be even greater if such an event occurs during a period of disproportionately heavy demand for our products or services or traffic on our systems or networks.

Providing disbursement services to higher education institutions is an emerging and uncertain business; if the market for our products does not continue to develop, we will not be able to grow this portion of our business.

Our success will depend, in part, on our ability to generate revenues by providing financial transaction services to higher education institutions and their students. The market for these services has only recently developed and the long-term viability and profitability of this market is unproven. Our business will be materially and adversely affected if we do not develop and market products and services that achieve and maintain market acceptance. Outsourcing disbursement services may not become as widespread in the higher education industry as we anticipate, and our products and services may not achieve continued commercial success. In addition, higher education institution clients could discontinue using our services and return to in-house disbursement and payment solutions. If outsourcing disbursement services do not become widespread or if higher education institution clients return to their prior methods of disbursement, our growth prospects, business, financial condition and results of operations could be materially and adversely affected.

Our business depends on a strong brand and a failure to maintain and develop our brand in a cost-effective manner may hurt our ability to expand our customer base.

Maintaining and developing the Higher One®, OneDisburse® and CASHNet® brands is critical to expanding and maintaining our base of higher education institution clients and student OneAccount holders. We believe the importance of brand recognition will increase as competition in our market further intensifies. Maintaining and developing our brands will depend largely on our ability to continue to provide high-quality products and services at cost effective and competitive prices, as well as after-sale customer

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service. While we intend to continue investing in our brands, we cannot predict the success of these investments. If we fail to maintain and enhance our brands, if we incur excessive expenses in this effort or if our reputation is otherwise tainted, including by association with the wider financial services industry, we may be unable to maintain loyalty among our existing customers or attract new customers, which could materially and adversely affect our business, financial condition and results of operations.

Our ability to generate revenue could suffer if we do not continue to update and improve our existing products and services and develop new ones.

The industry for electronic financial transactions, including disbursement services, is generally subject to rapid and significant technological changes, including continuing developments of technologies in the areas of smart cards, radio frequency and proximity payment devices (such as contactless cards), electronic commerce and mobile commerce, among others. While we cannot predict how these technological changes will affect our business, we believe that disbursement services to the higher education industry will be subject to a similar degree of technological change and that new services and technologies for the industry will emerge in the medium-term. As a result, these new services and technologies may be superior to, or render obsolete, the technologies we currently use in our products and services. In addition, the products and services we develop may not be able to compete with the alternatives available to our customers. Our future success will depend, in part, on our ability to adapt to technological changes and evolving industry standards.

We make substantial investments in improving our products and services, but we have no assurance that our investments will be successful. Our growth prospects, business, financial condition and results of operations will be materially and adversely affected if we do not develop products and services that achieve broad market acceptance with our current and potential customers.

Our business will suffer if we fail to successfully integrate acquired businesses and technologies or to appropriately assess the risks in particular transactions.

We have in the past acquired, and may in the future acquire, businesses, technologies, services, product lines and other assets. The successful integration of any business, technology, service, product line or other asset that we acquire in the future, on a cost-effective basis, may be critical to our future performance. If we do not successfully integrate a strategic acquisition, or if the benefits of the transaction do not meet the expectations of financial or industry analysts, the market price of our common stock may decline. The amount and timing of the expected benefits of any acquisition, including potential synergies between our current business and the acquired business, are subject to significant risks and uncertainties. These risks and uncertainties include, but are not limited to:

- the diversion of management s time and resources from our core business;
- our ability to retain or replace key personnel of the acquired business, including management and key sales force members;
- our ability to maintain relationships with the customers of the acquired business;
- our ability to integrate common disclosure controls and procedures, internal controls over financial reporting and accounting policies;
- the assumption of disclosed and undisclosed liabilities, including tax liabilities;
- the indemnification agreements with the sellers of the acquired business, under which we have made a claim against the former stockholders of IDC, may be unenforceable or insufficient to cover tax or other liabilities, see Part I, Item 3. Legal Proceedings of this report;

our ability to educate and train a combined sales force and cross-sell the combined products and services to our combined client base;

our ability to integrate the combined products, services and technology;

flaws in the acquired business technology;

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- inaccuracies in the acquired business books and records and any weaknesses in its internal controls;
- the existence of intellectual property infringement claims;
- our ability to coordinate organizations that are geographically diverse and that have different business cultures;
- our ability to integrate common legal, compliance, operational, financial and informational processes and systems; and
- our ability to comply with the regulatory requirements applicable to the acquired business.

As a result of these risks, we may not be able to achieve the expected benefits of any acquisition. If we are unsuccessful in completing an acquisition that we may pursue in the future, we would be required to reevaluate our growth strategy. Even if we successfully integrate other assets or businesses we may acquire, we may incur substantial expenses and devote significant management time and resources in seeking to complete and integrate the acquisition, the acquired businesses may not perform as we expect or enhance the value of our business as a whole.

We may be liable to our customers or lose customers if we provide poor service or if our systems or products experience failures.

We must fulfill our contractual obligations with respect to our products and services and maintain high quality service to meet the expectations of our customers. Failure to meet these expectations or fulfill our contractual obligations could cause us to lose customers and bear additional liability.

Because of the large amount of data we collect and manage, hardware failures and errors in our systems could result in data loss or corruption or cause the information that we collect to be incomplete or contain significant inaccuracies. For example, errors in our processing systems could delay disbursements or cause disbursements to be made in the wrong amounts or to the wrong person. Our systems may also experience service interruptions as a result of undetected errors or defects in our software, fire, natural disasters, power loss, disruptions in long distance or local telecommunications access, fraud, terrorism, accident or other similar reason, in which case we may experience delays in returning to full service, especially with regard to our data centers and customer service call centers. If problems such as these occur, our customers may seek compensation, withhold payments, seek full or partial refunds, terminate their agreements with us or initiate litigation or other dispute resolution procedures. In addition, we may be subject to claims made by third parties also affected by any of these problems.

Our ability to limit our liabilities by contract or through insurance may be ineffective or insufficient to cover our future liabilities.

We attempt to limit, by contract, our liability for damages arising from our negligence, errors, mistakes or security breaches. Contractual limitations on liability, however, may not be enforceable or may otherwise not provide sufficient protection to us from liability for damages. We maintain liability insurance coverage, including coverage for errors and omissions. It is possible, however, that claims could exceed the amount of our applicable insurance coverage, if any, or that this coverage may not continue to be available on acceptable terms or in sufficient amounts. Even if these claims do not result in liability to us, investigating and defending against them could be expensive and time consuming and could divert management s attention away from our operations. In addition, negative publicity caused by these events may delay market acceptance of our products and services, any of which could materially and adversely affect our reputation and our business.

If we are unable to protect or enforce our intellectual property rights, we may lose a competitive advantage and incur significant expenses.

Our business depends on certain registered and unregistered intellectual property rights and proprietary information. We rely on a combination of patent, copyright, trademark and trade secret laws, as well as nondisclosure agreements and technical measures (such as the password protection and encryption of our data and systems) to protect our technology and intellectual property rights, including our proprietary software. Existing laws afford only limited protection for our intellectual property rights. Intellectual property rights or registrations granted to us may provide an inadequate competitive advantage to us or be too narrow to protect our products and services. Similarly, there is no guarantee that our pending applications for intellectual property protection will result in registrations or issued patents or sufficiently protect our rights. The protections outlined above may not be sufficient to prevent unauthorized use, misappropriation or disclosure of our intellectual property or technology and may not prevent our competitors from copying, infringing, or misappropriating our products and services. We cannot be certain that others will not independently develop, design around or otherwise acquire equivalent or superior technology or intellectual property rights. If we are unable to adequately protect our intellectual property rights, our business and growth prospects could be materially and adversely affected.

One or more of our issued patents or pending patent applications may be categorized as so-called business method patents. The general validity of software patents and business method patents has been challenged in a number of jurisdictions, including the United States. On June 28, 2010, the United States Supreme Court determined that a certain business method amounting to abstract ideas was not patentable. However, the Court stated that some business methods are patentable under the Patent Act, and reaffirmed that patent eligibility should be broad and open. Although the Court s decision provides little guidance on patentability of our business methods, our patents could become less valuable or unenforceable if additional requirements are imposed that our patents do not meet.

From time to time, we seek to enforce our intellectual property rights against third parties, such as through our current litigation against TouchNet Information Systems, Inc. See Part I, Item 3. Legal Proceedings of this report. The fact that we have intellectual property rights, including registered intellectual property, may not guarantee success in our attempts to enforce these rights against third parties. Our ability and potential success in enforcing our rights is also subject to general litigation risks, as well as uncertainty as to the enforceability of our intellectual property rights. When we seek to enforce our rights, we may be subject to claims that our intellectual property rights are invalid, otherwise unenforceable, or are licensed to the party against whom we are asserting the claim. In addition, our assertions of intellectual property rights may result in the other party seeking to assert various claims against us, including its own alleged intellectual property rights, claims of unfair competition, or other claims. Furthermore, enforcing our intellectual property and other proprietary rights can be expensive. Any increase in the unauthorized use of our intellectual property could make it more expensive or less profitable to do business and consequently have a material adverse effect on our business, financial condition and results of operations.

As a holding company, our main source of cash is distributions from our operating subsidiaries.

We, Higher One Holdings, Inc., conduct all of our operations through our subsidiaries. Accordingly, our main cash source is dividends and other distributions from these subsidiaries. The ability of each subsidiary to make distributions depends on the funds that a subsidiary has from its operations in excess of the funds necessary for its operations, obligations or other business plans. Since our subsidiaries are wholly owned by us, our claims will generally rank junior to all other obligations of the subsidiaries. If our operating subsidiaries are unable to make distributions, we may not be able to implement our growth strategy, unless we are able to obtain additional debt or equity financing. In the event of a subsidiary s liquidation, there may not be assets sufficient for us to recoup our investment in the subsidiary.

Failure to establish and maintain effective internal controls over financial reporting may lead investors to lose confidence in our financial data.

Maintaining effective internal controls over financial reporting is necessary for us to produce reliable financial reports and is important in helping to prevent financial fraud. We are in the process of

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evaluating how to document and test our internal control procedures to satisfy the requirements of Section 404 of Sarbanes-Oxley and the related rules of the SEC which require, among other things, our management to assess annually the effectiveness of our internal control over financial reporting and our independent registered public accounting firm to issue a report on our internal control over financial reporting beginning with our Annual Report on Form 10-K for the year ending December 31, 2011. During the course of this documentation and testing, we may identify deficiencies that we may be unable to remedy before the requisite deadline for those reports.

For example, in connection with the preparation of our quarterly financial statements as of and for the three months ended March 31, 2010, we concluded that we had a material weakness in our internal control over financial reporting that resulted in a misstatement of our earnings per share computation for the year ended December 31, 2008. Specifically, in our computation of net income available to common stockholders per common share, we did not deduct from net income the difference between (i) the fair value of the consideration transferred to the preferred stockholders as part of our 2008 stock tender offer and (ii) the carrying amount of the preferred stock repurchased (net of issuance costs) to arrive at income available to common stockholders in accordance with FASB ASC 260-10-S99. As a result, we determined that we did not maintain effective controls over the accounting for, and calculation of, net income available to common stockholders per common share, indicating a material weakness with respect to our ability to properly monitor and account for non-routine transactions, and to apply GAAP in transactions subject to complex accounting pronouncements.

During 2010, we remediated this material weakness by, among other things, expanding our current finance and accounting staff, formalizing our accounting policies and internal controls documentation and strengthening supervisory reviews by our management. We cannot be certain that we will not fail to identify a new material weakness or that we will otherwise maintain effective internal controls over financial reporting in the future. If we are unable to maintain effective internal controls over financial reporting, it could result in a material misstatement of our financial statements that would not be prevented or detected on a timely basis and which could cause investors to lose confidence in our financial information and/or cause the price of our common stock to decline.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

We do not own any real property. Our corporate headquarters is located in New Haven, Connecticut, where we lease approximately 60,665 square feet of general office space pursuant to a lease which is currently due to expire on July 31, 2011.

We also have operations in Oakland, California, where we lease approximately 11,760 square feet of general office space pursuant to a lease which is currently due to expire on January 31, 2016.

We believe that our facilities are generally adequate for our current use. We anticipate that we will require additional space in the future and that this additional space will be available as needed. We expect to be able to extend our lease in New Haven as needed until our new headquarters are ready for occupancy. See Part II, Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources Cash Flows Investing Activities Real Estate Development Project of this report.

Item 3. Legal Proceedings

We, and our subsidiaries, are involved in legal proceedings concerning matters arising in the ordinary course of our business, including the matters described below. Although the outcome of such proceedings, including the matters described below, cannot be predicted with certainty, management

does not believe that the ultimate resolution of these matters will have a material adverse effect on our business, financial condition or results of operations.

In February 2009 and September 2010, Higher One, Inc. filed two separate complaints against TouchNet Information Systems, Inc., or TouchNet, in the United States District Court for the District of Connecticut alleging patent infringement related to TouchNet s offering for sale and sales of its eRefund product in violation of two of our patents. In the complaints, we sought judgments that TouchNet has infringed two of our patents, a judgment that TouchNet pay damages and interest on damages to compensate us for infringement, an award of our costs in connection with these actions and an injunction barring TouchNet from further infringing our patents. TouchNet answered the complaint and asserted a number of defenses and counterclaims, including that it does not infringe our patent, that our patent is invalid or unenforceable and certain allegations of unfair competition and state and federal antitrust violations. In addition, TouchNet s counterclaims sought dismissal of our claims with prejudice, declaratory judgment that TouchNet does not infringe our patent and that our patent is invalid or unenforceable, as well as an award of fees and costs related to the action, and an injunction permanently enjoining us from suing TouchNet regarding infringement of our patent. The parties are currently in the discovery stage of the proceeding. We intend to pursue the matter vigorously. There can be no assurances of our success in these proceedings.

On June 22, 2010, Higher One, Inc. provided notice and a certificate of claim for indemnity under the Stock Purchase Agreement by and among us and the former stockholders of IDC dated November 19, 2009, arising from certain misrepresentations and breaches of warranty. At the same time, we deposited $8.25 million, equal to the remaining balance of the post-closing payments, with an escrow agent. The funds held in escrow are shown on the balance sheet included in the audited financial statements included elsewhere in this report as restricted cash pending resolution of the outstanding claims.

Separately, the former stockholders of IDC filed a complaint against Higher One, Inc. in the United States District Court for the Northern District of California on July 20, 2010 (which we refer to as the Complaint), disputing that misrepresentations were made and that warranties were breached; alleging breach of contract and anticipatory breach; and seeking a declaratory judgment ordering that the post-closing payments be made in accordance with the schedule set forth in the Stock Purchase Agreement. On October 27, 2010, we filed a motion to dismiss and, in the alternative, to move the action to the District of Delaware pursuant to a contractual forum selection clause and to strike certain allegations of the complaint. On December 21, 2010, the court denied the motion as to dismissal or transfer, but agreed to strike the former stockholders request for a jury trial. We answered the Complaint on January 14, 2011, and also alleged counterclaims for breach of contract, negligent misrepresentation, and fraud. On February 7, 2011, the former stockholders moved to dismiss the counterclaims for fraud and misrepresentation only. That motion is currently being litigated. We intend to vigorously defend against the Complaint brought against us and to vigorously pursue our counterclaims. There can be no assurances of our success in these matters. As of December 31, 2010, the acquisition payable of $8.25 million was recorded as a liability on the balance sheet included in the audited financial statements included elsewhere in this report. We have not recorded any potential gain or loss in connection with this claim.

Following a recently conducted compliance examination, the New York Regional Office of the FDIC notified us that it is prepared to recommend to the Director of FDIC Supervision that an enforcement action be taken against us for alleged violations of certain applicable laws and regulations principally relating to our compliance management system and policies and practices for past overdraft charging which we believe to have impacted persistently delinquent accounts, which is a small percentage of our total accounts, collections and transaction error resolution. Any such enforcement action could result in an order to pay restitution and civil money penalties. We are in the process of responding to the FDIC s notification and we believe that we have voluntarily either remedied or taken steps to correct the alleged violations, but there can be no assurances as to the outcome of this process. An action instituted against us that results in significant changes to practice, the imposition on us of fines or penalties, or an obligation for us to pay restitution and civil money penalties could have a material adverse effect on our business, financial

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condition and results of operations.

Item 4. Submission of Matters to a Vote of Security Holders

No matters were submitted to security holders for a vote during the quarter ended December 31, 2010.

PART II

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

Our common stock is quoted on New York Stock Exchange under the symbol ONE. Prior to June 17, 2010 our common stock was privately held and did not trade on any exchange. The following table sets forth, for each of the periods indicated, the high and low reported sales price at close of our common stock on the NYSE.

	High	Low
Year ended December 31, 2010		
Fourth Quarter	$ 21.87	$ 15.54
Third Quarter	16.49	11.30
Second Quarter (Beginning June 17)	15.15	14.27
First Quarter		
Year ended December 31, 2009		
Fourth Quarter		
Third Quarter		
Second Quarter		
First Quarter		

As of February 18, 2011, we had 169 stockholders of record of our common stock. The closing sale price of our common stock on February 18, 2011 was $19.39 per share.

We have not paid any cash dividends on our common stock during the years ended December 31, 2010 or 2009. The payment of future cash dividends is within the discretion of our board of directors and will depend upon our future earnings, if any, our capital requirements, financial condition and other relevant factors. See Note 10 of notes to our consolidated financial statements for a description of restrictions on our ability to pay dividends.

The outstanding options and restricted shares are not transferable for consideration and do not have dividend equivalent rights attached.

Securities Authorized For Issuance Under Equity Compensation Plans

For information regarding securities authorized for issuance under equity compensation plans, see Part III, Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters of this report.

Stockholder Return Performance Presentation

The following graph compares the change in the cumulative total stockholder return on our common stock during the period from June 17, 2010 (the first day our stock began trading on the NYSE) through December 31, 2010, with the cumulative total return on the S&P 500 Index and the S&P 500 Financials Index. The comparison assumes that $100 was invested on June 17, 2010 in our common

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stock and in each of the foregoing indices and assumes reinvestment of dividends, if any.

Use of Proceeds from Public Offering of Common Stock

On June 16, 2010, our registration statement (File No. 333-165673) was declared effective for our initial public offering, pursuant to which we registered the offering and sale of 3,103,822 shares of common stock by Higher One Holdings, Inc. and the associated sale of 5,896,178 shares of common stock by selling shareholders and the additional sale pursuant to the underwriters over-allotment option for an additional 465,573 shares of common stock by us and an additional 884,427 by selling shareholders at a public offering price of $12.00 per share. The offering closed on June 22, 2010. The managing underwriter was Goldman, Sachs & Co.

The aggregate public offering price of the offering amount registered was $124.2 million and the offering did not terminate before all of the shares registered in the registration statement were sold. Our proceeds of $37.2 million, net of issuance costs of $5.6 million were used to pay outstanding amounts on the credit facility of $18 million, make an escrow payment of $8.3 million related to the acquisition payable and fund working capital. We did not receive any of the proceeds from the sale of shares by the selling stockholders. We anticipate that we will use the remaining net proceeds from our initial public offering for working capital and other general corporate purposes, which may include the acquisition of other businesses, products or technologies. We do not, however, have agreements or commitments for any specific acquisitions at this time. Pending such uses, we have and plan to continue to invest the net proceeds in short-term, interest-bearing, investment grade securities.

Item 6. Selected Financial Data

You should read the data set forth below in conjunction with Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations , our consolidated financial statements and related notes and other financial information included elsewhere in this report. We derived the selected financial data as of December 31, 2009 and 2010 and for each of the three years ended December 31, 2008, 2009 and 2010 from our audited consolidated financial statements and the related notes appearing elsewhere in this report. We have revised our consolidated statements of operations for immaterial errors for the year ended December 31, 2009 and our quarterly results during the years ended December 31, 2009 and 2010 to increase account revenue and cost of revenue for certain interchange income that was previously reflected as a reduction in cost of revenue, rather than as account revenue. This revision has no impact on the Company s gross margin, net income or cash flows. This error was inconsequential for

the year ended December 31, 2008. Account revenue and cost of revenue were each increased by $2,089 for the year ended December 31, 2009. Account revenue and cost of revenue were each increased by $3,452 for the nine months ended September 30, 2010. We derived the selected financial data as of and for the years ended December 31, 2006 and 2007 and as of December 31, 2008 from our audited financial statements and the related notes not included in this report.

Consolidated Statement of Income Data

	Year Ended December 31,				
	2006	2007	2008	2009	2010
	(in thousands, except share and per share amounts)				
Revenue	$ 16,006	$ 27,978	$ 44,006	$ 77,606	$ 144,969
Cost of revenue	6,569	11,140	16,302	26,529	51,845
Gross margin	9,437	16,838	27,704	51,077	93,124
Operating expenses	9,268	12,625	17,753	28,396	51,877
Income from operations	169	4,213	9,951	22,681	41,247
Other expense	(503)	(569)	(26)	(537)	(700)
Income before income taxes	(334)	3,644	9,925	22,144	40,547
Income tax (benefit) expense	(3,689)	1,362	3,547	7,925	15,488
Net income	3,355	2,282	6,378	14,219	25,059
Less: Effect of redemption of preferred stock			80,744		
Less: Net income allocable to participating securities	2,657	1,808		11,477	8,910
Net income (loss) available to common shareholders	$ 698	$ 474	$ (74,366)	$ 2,742	$ 16,149
Net income (loss) per common share:					
Basic	$ 0.06	$ 0.04	$ (7.22)	$ 0.29	$ 0.48
Diluted	0.06	0.04	(7.22)	0.27	0.44
Weighted average common shares outstanding:					
Basic	10,927,089	10,957,833	10,306,392	9,298,131	33,395,310
Diluted	55,801,845	57,090,867	10,306,392	53,150,890	57,302,843

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Consolidated Balance Sheet Data

	As of December 31,				
	2006	2007	2008	2009	2010
			(in thousands)		
Cash and cash equivalents	$ 5,770	$ 9,755	$ 1,488	$ 3,339	$ 34,484
Total assets	13,974	18,423	13,665	58,695	119,441
Total debt and capital lease obligations, including current maturities	950	1,172	18,934	27,647	8,250
Total liabilities	20,740	22,675	25,402	51,589	36,050
Total stockholders (deficit) equity	(6,766)	(4,252)	(11,737)	7,106	83,391

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

In addition to historical information, this report contains forward-looking statements that involve risks and uncertainties, which may cause our actual results to differ materially from plans and results discussed in forward-looking statements. We encourage you to review the risks and uncertainties, discussed in the section entitled Risk Factors, in Part I, Item 1A of this report, and the note regarding Forward-Looking Statements , included at the beginning of this report. The risks and uncertainties can cause actual results to differ significantly from those forecasted in forward-looking statements or implied in historical results and trends.

The following discussion should be read in conjunction with our consolidated financial statements and related notes appearing elsewhere in this report.

Overview

We believe that based on market share and the number of campuses employing our products, we are a leading provider of technology and payment services to the higher education industry. We believe that none of our competitors can match our ability to provide solutions for higher education institutions financial services needs, including compliance monitoring, and, consequently, that we provide the most comprehensive suite of disbursement and payment solutions specifically designed for higher education institutions and their students. We also provide campus communities with convenient, cost-competitive and student-oriented banking services, which include extensive user-friendly features.

Our products and services for our higher education institutional clients include our OneDisburse® Refund Management® disbursement service and our suite of payment transaction products and services. Through our bank partner, we offer our OneAccount service to the students of our higher education institutional clients, which includes an FDIC-insured deposit account, a OneCard, which is a debit MasterCard® ATM card, and other retail banking services.

As of December 31, 2010, over 430 campuses serving approximately 3.3 million students had purchased the OneDisburse® service and over 330 campuses serving approximately 2.5 million students had contracted to use one or more of our payment products and services. We also had approximately 1.6 million OneAccounts.

For the year ended December 31, 2010:

- total revenue was approximately $145.0 million, representing three-year compounded annual growth of approximately 73%;

- adjusted EBITDA was approximately $59.5 million, representing three-year compounded annual growth of approximately 121%;

- adjusted net income was approximately $34.4 million representing three-year compounded annual growth of approximately 142%;

net income was approximately $25.1 million, representing three-year compounded annual growth of approximately 122%.
See Supplemental Non-GAAP Financial and Operating Information below for definitions of

EBITDA and adjusted EBITDA and adjusted net income (each non-GAAP measures) and reconciliations to net income.

In addition, as of December 31, 2010, the number of OneAccounts had increased by a compounded annual growth rate of 65% compared to December 31, 2007.

We expect our growth to continue in the future and that our strategy will continue to offer significant opportunity for expansion. Our growth strategy includes the following elements:

- Expanding the number of contracted higher education institutions;
- Increasing OneAccount adoption and usage rates;
- Cross-selling our products to existing clients to increase the number of institutions using each product;
- Enhancing our products and services to create new sources of revenue; and
- Pursuing strategic partnerships and opportunistic acquisitions.

In evaluating our results, we consider a variety of operating and financial measures. The key metrics that we use to determine how our business is performing include: (i) total number of students enrolled at our higher education institutional clients; (ii) number of active OneAccounts; (iii) total revenue; (iv) adjusted EBITDA; (v) adjusted net income; and (vi) net income. See Supplemental Non-GAAP Financial and Operating Information below for definitions of EBITDA and adjusted EBITDA and adjusted net income (each non-GAAP measures) and reconciliations to net income.

Our primary source of revenue is generated from the use of OneAccounts. The primary factor affecting our revenue is the number of active OneAccounts, which, in turn, is significantly affected by the total number of students enrolled at a higher education institutional client.

Revenue

We derive revenue primarily from fees charged for the transactions that we facilitate for our higher education institutional clients and our banking customers. Most of these fees are charged on a per transaction basis and, accordingly, transaction volumes significantly affect our revenue growth. Transaction volumes are generally a function of the number of students enrolled at each of our higher education institutional clients, as larger student populations lead to greater numbers of active OneAccounts and related banking transactions, as well as other transactions such as OneDisburse®-based disbursements and payment transactions.

Generally, we negotiate with our higher education institutional clients the fee rates we charge them. Fees charged to our banking and payment transaction customers are generally set by a schedule and apply unilaterally to all customers. Fees charged for OneAccount services are collected by our bank partner as incurred and subsequently remitted to us. Fees charged on payment transactions are charged as incurred and retained by us, while fees charged in respect of our OneDisburse® product are billed to our higher education institutional clients and subsequently collected from them.

We believe our revenue stream is relatively stable, recurring and predictable, as the majority of our revenue each year is generated through existing relationships with higher education institutions and their campus communities. For example, in 2010, including revenue generated by customers acquired through our acquisition of IDC, which we renamed Higher One Payments, Inc., in November 2009, we generated over 90% of our revenue from contracts signed in prior years. In addition, our experience is that OneAccount, disbursement and payment transaction volumes and patterns are generally similar from one period to another, resulting in a large degree of predictability.

Our approximately 98% retention rate since 2003 among our higher education institutional clients, including CASHNet clients, also helps to ensure a relatively stable, recurring and predictable revenue stream.

We divide our revenue into four categories: account revenue, payment transaction revenue, higher

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education institution revenue and other revenue.

Account Revenue

We generate revenue from active OneAccounts, which are opened and funded by students and other members of the campus community. The OneAccount offered to our customers has no monthly fee or minimum balance requirement. We earn revenue based on both interchange fees and account service fees. Account service fees include, for example, foreign ATM fees and non-sufficient fund fees. These fees are either charged by our bank partner and remitted to us or we charge them to our clients directly. In December 2010, we began to offer a new version of the OneAccount that has a different fee schedule compared to the original OneAccount, including a monthly fee that is waived if certain activity requirements are met.

Our bank partner charges merchants interchange fees for point-of-sale, or POS, purchases made with OneCards and remits these fees to us. The amount of the fee generally depends on the size of the transaction, the merchant where the purchase is made and the network through which the transaction is processed.

We earn ATM fees from transactions conducted through our ATMs with cards other than OneCards. We also earn fees from ATM transactions conducted by OneAccount holders using their OneCards at ATMs outside of our ATM network.

Our bank partner charges NSF fees and remits them to us when OneAccount holders attempt to withdraw or transfer money from their OneAccounts in excess of their deposited funds. These NSF fees are primarily assessed on electronic transfers from, and checks drawn on, accounts in excess of available funds. Historically, our bank partner also assessed these fees on overdrafts on debit card transactions. However, the Federal Reserve Board amended Regulation E to limit the ability of financial institutions, effective July 1, 2010, to assess an overdraft fee for paying ATM and one-time debit card transactions that overdraw a consumer s account, unless the consumer affirmatively consents, or opts in, to the institution s payment of overdrafts for these services. We do not currently offer the opt in feature to our customers for ATM or one-time debit card transactions. In the absence of debit card-related NSF fees, our total NSF fees per OneAccount that our bank partner remits to us began to decrease during 2010 and is expected to continue to decrease on a comparative basis until August 2011. A portion of this decrease in total revenue has been offset by a reduction in our provision for operational losses, which is recorded in cost of revenue. This is due to a reduction in our overdraft liability and the amount of our estimated uncollectible fees. See Notes 2 and 8 to our consolidated financial statements included elsewhere in this report.

We earn other fees for banking services provided to OneAccount holders, including fees for conducting wire transfers, replacing lost OneCards, processing international transactions, processing stop payment requests, over-the-counter cash withdrawals using OneCards, issuing official checks and electronic bill pay features.

While our historical experience has been that account revenue generated per OneAccount has been generally stable year over year, with total account revenue generally increasing proportionally with increases in the number of OneAccounts, the implementation of Regulation E in the third quarter of 2010 along with other changes that we made to our account fee schedule, decreased the revenue per OneAccount in that period compared to the same period in the prior year. This continued into the fourth quarter of 2010, and we expect account revenue per OneAccount to continue to be lower in 2011 compared to previous periods as the result of non-sufficient funds fee changes made in response to regulations and other changes we made through the third quarter of 2011. Notwithstanding the decrease in non-sufficient fund fees, the primary influence on account revenue growth is expected to continue to be the number of active OneAccounts. Growth in the number of accounts is tied to growth in the number of students enrolled at our OneDisburse® higher education institutional clients, which expands as new clients contract to use this product. The average percentage of students that maintain OneAccounts at a higher education institution generally increases over the first several years after the higher education institution becomes a OneDisburse® client. We believe the rate of OneAccount adoption varies, however, based on factors including, but not limited to, the average tenure of a student at a higher education institution,

whether the higher education institution is a 2-year or a 4-year school or a public or private school and the mix of undergraduate and graduate students.

The number of OneAccounts has risen in each of the last three years, which has led to a compounded annual growth rate of 72% in account revenue over this period. While we expect the number of OneAccounts to continue to grow in the near-term, there is a possibility that further legislative and regulatory changes will be enacted in the near-term that may reduce account revenue. See Part I, Item 1A. Risk Factors Fees for financial services are subject to increasingly intense legislative and regulatory scrutiny, which could have a material adverse effect on our business, financial condition, results of operations and prospects for future growth of this report.

Payment Transaction Revenue

We generate payment transaction revenue through convenience fees charged to students, parents or other payers who make online payments to our higher education institutional clients through the SmartPay feature of our ePayment product using a credit or debit card. As this fee is assessed on a per transaction basis, growth in payment transaction revenue is primarily influenced by transaction volumes. We acquired ePayment when we purchased IDC in November 2009.

Higher Education Institution Revenue

Our higher education institutional clients pay fees for the products and services they purchase from us. We charge our clients: (i) an annual subscription fee based on the size of their student population; (ii) a per-transaction fee; or (iii) a combination of both. For certain payment transaction products, we also charge an implementation fee, which is deferred and recognized over the estimated client relationship period, which we estimate to be five years. Historically, revenue from higher education institutions has been primarily comprised of carding and transaction fees related to our OneDisburse® product. However, with our acquisition of IDC in November 2009, the composition of our higher education institution revenue changed substantially, with a large proportion of this revenue stream to being derived from our payment products-related revenue.

The number of students enrolled at client institutions and the number of campuses under contract are significant drivers of our higher education institution revenue. As we have expanded the number of our institutional clients over the last three years, our higher education institution revenue has grown by a compounded annual rate of 87%. We expect that assuming our institutional client base grows, our higher education institution revenue will also increase.

Other Revenue

Other revenue consists of two main components: a marketing incentive fee paid by MasterCard International Incorporated based on transaction volumes and new OneCard issuances and processing fees paid by our bank partner based on the total amount of deposits held in our OneAccounts and prevailing interest rates. Because the amount of the processing fee is in part a function of prevailing interest rates, this revenue stream has historically fluctuated in accordance with interest rate movements. Since 2008, fees paid by our bank partner have been relatively small due to low interest rates. If prevailing interest rates rise our processing fee will also increase. Currently, this revenue stream is immaterial to our overall results of operations.

Cost and Expenses

Employee compensation and related expenses represent our largest single expense. We allocate compensation and other related expenses, including stock-based compensation, to cost of revenue, product development, sales and marketing and general and administrative expenses. While we expect the number of our employees to increase over time, we believe the economies of scale in our business model will allow us to grow our compensation and related expenses at a lower rate than revenue.

Other costs and expenses include outsourced managed hosting, data processing, ATM-related expenses, professional services, office lease payments, travel and amortization.

The following summarizes our cost of revenue and certain significant operating expenses:

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Cost of Revenue

Cost of revenue consists primarily of data processing expenses, interchange expenses related to SmartPay and ATM transactions, uncollectible fees and write-offs and customer service expenses. These expenses are shared across our different revenue categories and we are not able to meaningfully allocate such costs between separate categories of revenue. Consequently, all costs and expenses applicable to our revenue are included in the cost of revenue category in our statements of operations. These expenses generally move in line with the number of active OneAccounts and transaction volumes for our banking and payment transactions services.

General and Administrative

General and administrative expenses include finance, legal, compliance, facility and administration costs, as well as components of operational costs such as ATM cash services and maintenance, data center costs and costs associated with our information technology. These costs include employee compensation and related expenses, as well as fees for professional services. As a newly public company, we have started to incur additional general and administrative expenses as a result of our obligations to comply with the ongoing obligations of a public company, including the SEC s ongoing reporting obligations, director and officer liability insurance and other expenses.

Product Development

Product development expenses include costs associated with defining and specifying new features and ongoing enhancements for our proprietary technology platform and other aspects of our service offerings. Product development costs primarily relate to employee compensation.

Sales and Marketing

Sales and marketing expenses include costs of acquiring new institutional clients and educating their students about our services in order to improve the adoption and usage rates of our OneAccount and our other student-oriented products and services. The majority of our sales and marketing expenses are comprised of employee compensation. Each of our sales representatives earns: (i) a base salary; (ii) sales commissions, which are earned upon the signing of a contract with a higher education institutional client; and (iii) generally, certain trailing commissions, which are based on account performance. Having nearly doubled the number of our sales and marketing personnel with our acquisition of IDC, our sales and marketing expense increased significantly during 2010.

We record stock-based customer acquisition expense in connection with the EduCard acquisition from 2008 and pursuant to a related intellectual property purchase agreement. The amount of stock-based customer acquisition expense depends on the number of shares released from escrow to Kevin Jones and the value of the shares at that time. We also record cash-based customer acquisition expense in connection with our acquisition of IDC in November of 2009.

IDC Acquisition

In November of 2009, we acquired IDC, a leader in providing cashiering and payment solutions in higher education, which we renamed Higher One Payments, Inc. This transaction provided us with our suite of payment transaction products and services, the capability to offer our higher education institutional clients a full complement of services and nearly doubled the number of campuses with which we have relationships. At the time of the acquisition there was only a 6% overlap of students enrolled at institutions that were clients using both Higher One® and IDC products and services. Our overlap has increased to approximately 9% as of December 31, 2010 and we expect our overlap to continue to increase in the future as a result of future cross-sales.

We purchased IDC for $27.5 million, which was financed by cash and debt. At closing, we paid an initial payment of $17.6 million that was funded with $9.9 million of available cash and $7.7 million of borrowings under our existing credit line. The remaining non-interest bearing post-closing payment of $10 million was due to the former shareholders in quarterly payments through December 31, 2010. During 2010, we made one payment of $1.75 million to the former shareholders and deposited the remaining $8.25 million in an escrow account, which amount remains the subject of an ongoing dispute. See also

Part I, Item 3. Legal Proceedings of this report.

In acquiring IDC, we purchased its payment transaction suite of products and services, such as ePayment, eBill, MyPaymentPlan, eMarket and Cashiering, which we did not previously offer. See also Part I, Item 1. Business Products and Services Payment Suite of this report.

Critical Accounting Policies

A number of our accounting policies require the application of significant judgment by our management, and such judgments are reflected in the amounts reported in our consolidated financial statements. In applying these policies, our management uses its judgment to determine the appropriate assumptions to be used in the determination of estimates. Those estimates are based on our historical experience, terms of existing contracts, management s observation of trends in the industry and information available from other outside sources, as appropriate. On an ongoing basis, we evaluate our estimates and judgments. Actual results may differ significantly from the estimates contained in our consolidated financial statements. We believe that the following are our critical accounting policies.

Provision for Operational Losses

We have entered into an agreement with The Bancorp Bank to hold all deposit accounts opened by OneAccount holders. Although those deposit funds are held by The Bancorp Bank, we are liable to the bank for any uncollectible accountholder overdrafts and any other losses due to fraud or theft. We provide reserves for our estimated overdraft liability and our estimated uncollectible fees to The Bancorp Bank. The provision for these reserves is included within the costs of revenue on the consolidated financial statements included in this report. Such reserve is based upon an analysis of outstanding overdrafts and historical repayment rates. For the years ended December 31, 2008, 2009 and 2010, we provided for additional reserves for operational losses related to uncollectible accountholder overdrafts of $4.6 million, $5.5 million and $7.2 million, respectively. If the financial condition of the accountholders were to deteriorate, thereby reducing their ability to make payments, additional reserves would be required.

Goodwill and Intangible Assets

Goodwill represents costs in excess of the fair value of consideration transferred over the fair values assigned to the underlying net identifiable assets of acquired businesses. Annual impairment testing of goodwill is assessed in accordance with FASB ASC 350, Intangibles Goodwill and Other, or ASC 350, which compares carrying values of the reporting units to fair values and, when appropriate, the carrying value of these assets is reduced to fair value.

Our goodwill balance is entirely attributable to our acquisition of IDC on November 19, 2009. We perform our annual goodwill impairment analysis as of October 31, or whenever events or changes in circumstances indicate that an impairment may have occurred.

We determined our reporting units in accordance with FASB ASC 280 Segment Reporting , or ASC 280, and ASC 350. We evaluate reporting units by first identifying their operating segments under ASC 280. We then evaluate each operating segment to determine if it includes one or more components that constitute a business. If there are components within an operating segment that meet the definition of a business, we evaluate those components to determine if they must be aggregated into one or more reporting units. When determining if it is appropriate to aggregate a newly acquired operating segment with our existing operating segment, we evaluate the seller s historical results for the newly acquired company and its future prospects. This evaluation generally includes the newly acquired operating segment s budget and the actions that our management expects to take with respect to the recently acquired operating segment, as well as an evaluation of the likelihood that such actions will be implemented. If, after evaluating the future prospects, we determine that the two segments are economically similar within a reasonable period of time, the two operating segments are aggregated. We have one operating segment and reporting unit.

Impairment may result from, among other things, deterioration in the performance of the acquired business, adverse market conditions, adverse changes in applicable laws or regulations, including

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changes that restrict the activities of the acquired business, and a variety of other circumstances. Actual cash flows arising from a particular reporting unit could vary from projected cash flows, which could imply different carrying values from those established at the date of acquisition, and which could result in impairment of such assets. If it is determined that an impairment has occurred, we would record a write-down of the carrying value and charge the impairment as an operating expense in the period the determination is made. During 2009 and 2010, we were not required to record any impairment on goodwill or intangible assets. As of the completion of our impairment test on October 31, 2010, our reporting unit was not at risk of failing step one of the goodwill impairment test.

We assess the impairment of identifiable intangible assets and goodwill whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors we consider important which could trigger an impairment review include the following:

- significant underperformance relative to historical or projected future operating results;
- significant changes in the manner of our use of the acquired assets or the strategy for our overall business; and
- significant negative industry or economic trends.

When we determine that the carrying value of intangible assets may not be recoverable based upon the existence of one or more of the above indicators of potential impairment, we assess whether an impairment has occurred based on whether net book value of the assets exceeds related projected undiscounted cash flows from these assets. We consider a number of factors, including past operating results, budgets, economic projections, market trends and product development cycles in estimating future cash flows. Differing estimates and assumptions as to any of the factors described above could result in a materially different impairment charge and thus materially different results of operations.

Stock-Based Compensation

We account for stock-based compensation expense in accordance with FASB ASC 718, *Compensation Stock Compensation*, or ASC 718, which requires the measurement and recognition of compensation expense for share-based awards based on the estimated fair value on the date of grant. The fair value of each option is estimated on the date of grant using the Black-Scholes option pricing model with the following range of assumptions for stock options granted during the years ended December 31, 2008, 2009 and 2010:

	2008	**2009**	**2010**
Expected term(1)	6.3 - 6.5 years	5.8 - 6.3 years	6.2 - 6.3 years
Expected volatility(2)	40.2%	50.7%	51.0 - 51.9%
Risk-free rate(3)	2.4% - 3.4%	2.2% - 3.2%	1.5% - 3.0%
Expected dividends(4)	None	None	None

(1) Expected term is the period of time that the equity grants are expected to remain outstanding. We calculate the expected life of the options as prescribed under the provisions of ASC 718. We generally use the midpoint between the end of the vesting period and the contractual life of the grant to estimate option exercise timing.
(2) Expected volatility is a measure of the amount by which a financial variable such as a share price has fluctuated (historical volatility) or is expected to fluctuate (expected volatility) during a period. We based our estimated volatility on the historical volatility of a peer group of publicly traded companies, which includes companies that are in the same industry or are our competitors.
(3) Risk-free rate is the average U.S. Treasury rate at the time of grant having a term that most closely approximates the expected term of the option.
(4) We have never declared or paid dividends on our common stock and do not anticipate paying

dividends in the foreseeable future.

These options expire ten years from the date of grant. Options for our employees vest over periods ranging from one month to five years, with the majority vesting as follows: one-fifth of the granted options vest one year from the date of grant; the remaining four-fifths vest at a rate of 1/48 per month over the remaining four years of the vesting period. The board grants primarily incentive stock options, but occasionally grants nonqualified stock options to key members of management.

The amount of stock based compensation expense we recognize during a period is based on the portion of the awards that are ultimately expected to vest. We estimate option forfeitures at the time of grant and revise those estimates in subsequent periods if actual forfeitures differ from those estimates.

Restricted stock is a stock award that entitles the holder to receive shares of our common stock as the award vests over time. The board has not granted restricted stock awards prior to 2009 when it granted a total of 43,344 shares to its executive officers. These awards vest over four years which start on the first anniversary of the grant. The fair value of each restricted stock award is estimated using the intrinsic value method that is based on the fair value of our common stock on the date of grant. Compensation expense for restricted stock awards is recognized ratably over the vesting period on a straight-line basis.

Generally, employees have received stock option grants when joining the company and then may have received periodic awards thereafter in the discretion of the board, although the timing of additional awards has previously not been made according to any established policy. The board intended all options to be granted with an exercise price equal to or greater than the per share fair value of our common stock underlying those options on the date of grant. On each of the grant dates during 2008, 2009 and up until our common stock offering in June 2010, the fair value of common stock underlying stock options granted was either estimated by the board on a contemporaneous basis with input from management and an independent valuation firm or was determined not to have changed since a prior valuation. Given the absence of a public trading market in our common stock through June 2010, our board considered numerous objective and subjective factors to determine the best estimate of the fair value of our common stock at each meeting at which stock option grants were approved. These factors included, but were not limited to, the following:

- developments in our business;
- issuances of our preferred stock;
- the rights and preferences of our convertible preferred stock relative to our common stock;
- independent valuations of our common stock;
- the lack of marketability of our common stock;
- the likelihood of achieving a liquidity event, given prevailing market conditions;
- the per share value of any recent preferred stock financing and the amount of convertible preferred stock liquidation preferences;
- our current and historical operating performance and current financial condition;
- our operating and financial projections;

- the stock price performance of a peer group comprised of selected publicly-traded companies identified as being comparable to us; and

- economic conditions and trends in the broad market for stocks.

If we had made different assumptions and estimates, the amount of our recognized and to be recognized stock-based compensation expense could have been materially different. We believe that the board used reasonable methodologies, approaches and assumptions in determining the fair value of our common stock.

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We requested periodic valuation reports from an independent valuation firm, prepared consistent with the methods outlined in the American Institute of Certified Public Accountants Practice Guide, Valuation of Privately-Held-Company Equity Securities Issued as Compensation in 2008, 2009 and up until our common stock offering in June 2010. Each valuation recommended a fair value of our common stock on a minority, non-marketable basis as of the date of the report.

In valuing our common stock, our independent valuation firm determined our business enterprise value using two valuation approaches, an income approach and a market approach.

The income approach estimates the present value of future estimated debt-free cash flows, based upon forecasted revenue and costs. These discounted cash flows are added to the present value of our estimated enterprise terminal value, the multiple of which is derived from comparable company market data. These future cash flows are discounted to their present values using a rate corresponding to our estimated weighted average cost of capital. The discount rate is derived from an analysis of the weighted average cost of capital of our publicly-traded peer group as well as cost of capital studies for similar stage companies as of the valuation date and is adjusted to reflect the risk inherent in our cash flows.

The market approach estimates the fair value of a company by applying to that company the market multiples of comparable publicly-traded companies. A multiple of key metrics implied by the enterprise values or acquisition values of our publicly-traded peers is calculated. Based on the range of these observed multiples, size of the company, company specific factors such as growth and margins, and professional judgment a appropriate adjustment to the publicly-traded companies median multiple is applied our metrics in order to derive an indication of value.

After determining a business enterprise value indication under each approach, the enterprise value was allocated to debt holders and then to each of our classes of stock using a liquidation analysis that took into consideration each class of shareholder s rights and preferences to proceeds. Under each of the value indications based on the shareholder agreements, the preferred shareholders would automatically convert to common shareholders. The two per share value indications were weighted to determine the concluded fair value of a share of common stock on a minority, non-marketable basis.

Upon our common stock offering in June 2010, we have relied upon on the trading price of our common stock to determine fair value of our common stock.

Grants in 2008, 2009 and 2010

With respect to equity grants made in 2008, 2009 and up until our common stock issuance in June 2010, the key assumptions in the common stock valuations recommended by an independent valuation firm were as follows:

Date of Valuation	Discounted Cash Flows Method / Guideline Public Company Weighting	Discount for Lack of Marketability	Discounted Cash Flow Discount Rate	Common Stock Value
December 31, 2008	75% / 25%	30%	20%	$ 3.43
June 30, 2009	75% / 25%	30%	20%	5.56
November 19, 2009	75% / 25%	20%	25%	10.80
March 15, 2010	75% / 25%	15%	23%	13.94

For purposes of the December 2008 and June 2009 valuations, the comparable publicly-traded companies utilized in the market approach consisted of Alliance Data Systems Corporation, CyberSource Corp., MasterCard Incorporated, TNS Inc. and Total Systems Services, Inc. The list was expanded to include Visa, Inc. in the November 2009 valuation report and to include Financial Engines, Inc. in the March 2010 valuation report.

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We have set forth in the table below information regarding stock options granted during 2009 and through May 2010. Following the table, we have described the significant factors contributing to our determinations of fair market value and setting of option exercise prices throughout this period.

Date of Grant	Number of Options Granted	Exercise Price	Option Fair Value
January 27, 2009	301,500	$ 4.59	$ 2.34
March 19, 2009	34,500	4.59	2.34
May 21, 2009	57,750	4.59	2.39
July 23, 2009	65,250	5.67	2.99
September 24, 2009	60,750	5.67	2.97
November 6, 2009	81,750	5.67	2.97
December 4, 2009	639,750	10.80	5.59
March 26, 2010	378,000	13.94	7.42
May 6, 2010	30,000	13.94	7.33

January, March and May 2009. On January 27, 2009, the board granted options with a strike price of $4.59 per share. We had received a valuation recommendation from the independent valuation firm of $3.43 as of December 30, 2008. However, the board had previously granted options in the second half of 2008 with a strike price of $4.59 per share. This price had been set based upon the per share sale price of Series E Convertible Preferred Shares to Lightyear Capital in August 2008. The board decided to grant options in January at the same strike price despite the lower third party stock valuation. The board continued to grant options on March 19 and May 21 utilizing the $4.59 strike price based upon the company s determination that the fair market value of the common stock had not increased above such price as a result of intervening events or changed financial conditions.

July through November 2009. On July 23, 2009, our board determined a fair market value of our common stock of $5.67 for purposes of setting exercise prices for options granted on that day. This determination was based on the factors described above, as well as the independent valuation firm s valuation recommendation of $5.56 in its June 30, 2009 report. The higher price in the report was a result of an increase in our enterprise value as determined under both the discounted cash flow method and the guideline public company method described above. In addition the terminal exit multiple increased based on the guideline public company multiple increase. The increase in value under the guideline public company method resulted primarily from an increase in the relevant multiple. The increase in value is reflected in the increase in revenue and adjusted EBITDA, which exceeded our 2009 plan. The board continued to grant options on September 24 and November 6 using the $5.67 strike price based on our determination that the fair market value of our common stock had not increased above such price as a result of intervening events or changed financial conditions.

December 2009. On December 4, 2009, the board determined a fair market value of our common stock of $10.80 for purposes of setting exercise prices for options granted on that day. This determination was based on the factors described above as well as the independent valuation firm s valuation recommendation of $10.80 in its November 19, 2009 report. Several factors contributed to the significant increase in value from the prior valuation in June 2009 including an increase in public comparables (42%), the value built by the company in the intervening six months as reflected in the increase in its revenue and adjusted EBITDA in excess of its 2009 business plan, the increased potential for an IPO based upon the stabilization of the financial markets and feedback from the company s investment bank and the increase in revenue and adjusted EBITDA as well as market and long-term growth potential resulting from its acquisition of IDC.

March 2010. On March 26, 2010, the board determined a fair market value of our common stock of $13.94 for purposes of setting exercise prices for options granted on that day. This determination was based on the factors described above as well as the independent valuation firm s valuation recommendation of $13.94 in its March 15, 2010 report. Several factors contributed to the increase in value from the prior valuation in November 2009. The company built value in the intervening period as

reflected in its exceeding the first two months of 2010 s operating plan in both revenue and adjusted EBITDA, in the significant growth in the trailing twelve month financials as of the valuation date compared to those as of October 2009 (32% revenue growth and 35% adjusted EBITDA growth) and significant new sales through the valuation date (49% of entire 2010 operating plan). In addition, the IPO liquidity potential continued to increase based upon feedback from the company s investment bank. Lastly, the acquisition of IDC continued to contribute to higher than projected results compared to the operating plan by adding new revenue and adjusted EBITDA to the combined financial projections, increasing the company s addressable market with university payments and the company s long-term growth potential and allowing for better than anticipated synergies and cross-selling.

May 2010. On May 6, 2010, consistent with its ordinary granting practices, the compensation committee granted an aggregate of 30,000 options to six new employees (none of whom are officers of the company) who were hired since the last meeting of our board of directors. The compensation committee set the exercise price for the options at $13.94, the same price used for options granted at its meeting six weeks earlier (as explained above). Consistent with its past practice and in light of the immaterial amount of options being granted, the compensation committee did not commission an independent valuation. In determining not to raise the exercise price, the compensation committee was influenced by the extreme volatility of the stock market on the date of grant and the effect it could have on other companies stock prices and on the timing of the offering, both of which play a role in the valuation of our stock.

After May 2010, the board set the exercise price for options granted based on the average of the high and low price of our common stock the day prior to the grant date.

Income Taxes

Deferred tax assets and liabilities are determined based on temporary differences between the financial reporting bases and the tax bases of assets and liabilities. Deferred tax assets are also recognized for tax net operating loss carry-forwards. These deferred tax assets and liabilities are measured using the enacted tax rates and laws that will be in effect when such amounts are expected to reverse or be utilized. The realization of total deferred tax assets is contingent upon the generation of future taxable income. Valuation allowances are provided to reduce such deferred tax assets to amounts more likely than not to be ultimately realized.

Income tax provision or benefit includes U.S. federal, and state and local income taxes and is based on pre-tax income or loss. In determining the estimated annual effective income tax rate, we analyze various factors, including projections of our annual earnings and taxing jurisdictions in which the earnings will be generated, the impact of state and local taxes and our ability to use tax credits and net operating loss carry-forwards.

Business Combinations

We follow the provisions of FASB ASC 805, Business Combinations, or ASC 805, which requires the acquiring entity in a business combination to recognize all the assets acquired and liabilities assumed in the transaction and establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed in a business combination.

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Results of Operations for the Years Ended December 31, 2008, 2009 and 2010

The following tables summarize key components of our results of operations for the periods indicated, both in dollars and as a percentage of total revenue:

	Year Ended December 31,			Change from prior period			
	2008	2009	2010	2009	2010	2009	2010
	(in thousands)			(in thousands of dollars)		(percentage)	
Account revenue	$ 37,570	$ 68,529	$ 113,516	$ 30,959	$ 44,987	82.4%	65.6%
Payment transaction revenue	29	1,688	15,742	1,659	14,054	5,720.7%	832.6%
Higher education institution revenue	3,220	5,135	12,543	1,915	7,408	59.5%	144.3%
Other revenue	3,187	2,254	3,168	(933)	914	(29.3%)	40.6%
Total revenue	44,006	77,606	144,969	33,600	67,363	76.4%	86.8%
Cost of revenue	16,302	26,529	51,845	10,227	25,316	62.7%	95.4%
Gross margin	27,704	51,077	93,124	23,373	42,047	84.4%	82.3%
General and administrative expense	11,725	18,143	32,381	6,418	14,238	54.7%	78.5%
Product development expense	1,629	2,287	3,311	658	1,024	40.4%	44.8%
Sales and marketing expense	4,399	7,966	16,185	3,567	8,219	81.1%	103.2%
Income from operations	9,951	22,681	41,247	12,730	18,566	127.9%	81.9%
Interest and other expense, net	412	558	729	146	171	35.4%	30.6%
Interest and other income, net	(386)	(21)	(29)	365	(8)	(94.6%)	38.1%
Income before income taxes	9,925	22,144	40,547	12,219	18,403	123.1%	83.1%
Income tax expense	3,547	7,925	15,488	4,378	7,563	123.4%	95.4%
Net income	$ 6,378	$ 14,219	$ 25,059	$ 7,841	$ 10,840	122.9%	76.2%

	Year Ended December 31,		
	2008	2009	2010
	(% of total revenue)		
Account revenue	85.4%	88.3%	78.3%
Payment transaction revenue	0.1%	2.2%	10.9%
Higher education institution revenue	7.3%	6.6%	8.7%
Other revenue	7.2%	2.9%	2.2%
Total revenue	100.0%	100.0%	100.0%
Cost of revenue	37.0%	34.2%	35.8%
Gross margin	63.0%	65.8%	64.2%
General and administrative expense	26.7%	23.4%	22.3%
Product development expense	3.7%	2.9%	2.3%
Sales and marketing expense	10.0%	10.3%	11.2%
Income from operations	22.6%	29.2%	28.5%
Interest and other expense, net	0.9%	0.7%	0.5%

Interest and other income, net	(0.9%)	0.0%	0.0%
Income before income taxes	22.6%	28.5%	28.0%
Income tax expense	8.1%	10.2%	10.7%
Net income	14.5%	18.3%	17.3%

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

Account revenue

The increase in account revenue was primarily due to an increase of 61.2%, or 0.6 million, in the number of OneAccounts from December 31, 2009 to December 31, 2010. Greater adoption of the OneAccount at existing higher education institution clients accounted for 47% of the increase in OneAccounts, while 53% of the increase was due to new higher education institution clients. The increase in the number of OneAccounts resulted in increases in interchange fees relating to point of sale purchases made with our OneCards, ATM fees, and other fees that our bank partner remitted to us. While our historical experience has been that account revenue generated per OneAccount has been generally stable year over year, with total account revenue generally increasing proportionally with increases in the number of OneAccounts, the implementation of Regulation E in the third quarter of 2010 as well as other changes we made to our fee schedule decreased the revenue per OneAccount compared to the same period in the prior year. This continued into the fourth quarter of 2010 and we expect the account revenue per OneAccount to continue to be lower than in previous periods as the result of non-sufficient funds fee changes made in response to regulations and other changes we made through the third quarter of 2011.

Payment Transaction Revenue

The increase in payment transaction revenue was primarily generated from our CASHNet® payment transaction products, which were added to our product offering with the acquisition of IDC in November 2009 and, accordingly, were only included in our payment transaction revenues for approximately one and one half months during the twelve months ended December 31, 2009.

Higher Education Institution Revenue

The increase in higher education institution revenue was primarily due to the inclusion of a full year of subscription and deployment revenue from our CASHNet® suite of products compared to only approximately 42 days of revenue in 2009.

Other Revenue

The increase in other revenue was primarily due to an increase of 26.6% in the marketing incentive fees payable to us from MasterCard due to higher MasterCard issuance incentives. An increase of 80.3% in processing fees that our bank partner paid to us, which resulted primarily from an increase in OneAccount deposits, also contributed to the growth in other revenue.

Cost of Revenue

The inclusion of processing fees related to our CASHNet® payment transaction revenue for the whole year in 2010, compared to only 42 days in 2009, accounted for $9.8 million, or 38.6% of the total growth in cost of revenue. Increases in data processing expenses of $4.6 million, or 67.8%, network fees and expenses of $2.7 million or 61.5% and customer service expenses of $2.0 million, or 61.1%, also contributed to the increase. The growth in these expenses was primarily due to a 61.2% increase in the number of active OneAccounts. An increase in amortization expense, primarily related to deferred implementation costs, of $2.0 million, or 132.1%, was driven by both new client implementations and the inclusion of costs resulting from our CASHNet® deployments. Write-offs and the provision for uncollectible fees increased $2.6 million, or 42.4%, driven by the increase in the number of active OneAccounts, which was partially offset by higher fee collection rates and lower aggregate overdrawn balances resulting from the implementation of amendments to Regulation E. The lower margin generally attained on the CASHNet® payment transaction revenue contributed to the 1.6% overall decrease in gross margin percentage.

General and Administrative Expense

The increase in general and administrative expense was driven primarily by increases of $6.8 million, or 69.2%, in employee compensation allocated to general and administrative expenses; $2.3 million, or 159.8%, in depreciation and amortization; and $1.5 million, or 107.9%, in information technology expenses. These expenses were the result of both the acquisition of IDC in November 2009

and of growth in our existing lines of business. Additionally, professional fees increased $1.3 million, or 106.3%, driven by growth in the size and complexity of our business and the additional costs of operating as a publicly traded company.

Product Development Expense

The increase in product development expense was primarily due to an increase in employee and outsourced costs primarily related to the addition of product development employees from CASHNet.

Sales and Marketing Expense

The increase in sales and marketing expense was primarily due to an increase of $4.9 million in the non-cash, stock-based sales acquisition expense related to the vesting of certain shares issued in connection with the acquisition of EduCard due to a higher average share price at the date of vesting. Increases in costs related to employee compensation of $2.1 million, primarily related to the addition of employees from Higher One Payments, Inc., and cash-based sales acquisition expense related to the acquisition of IDC of $0.7 million also contributed to the overall increase.

Interest Expense

The increase in interest expense was primarily due to the accretion of interest related to the acquisition payable incurred as a result of the IDC acquisition in November 2009 and amortization of financing costs associated with amending the credit facility in July and December of 2009.

Income Tax Expense

The increase in income tax expense was primarily due to an increase of $18.4 million, or 83.1%, in net income before taxes and also a higher effective state tax rate. The effective tax rates for the years ended December 31, 2009 and 2010 were 35.8% and 38.2%, respectively.

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

Account revenue

The increase in account revenue was primarily due to an increase of 81.2% in the number of OneAccounts compared to the previous year, which resulted in increases in interchange fees that our bank partner remitted to us and relating to POS purchases made with our OneCards, ATM fees and NSF fees that our bank partner remitted to us.

Payment Transaction Revenue

Payment transaction revenue was $1.7 million for the year ended December 31, 2009, which was primarily generated by the inclusion of 42 days of revenue generated by our CASHNet payment transaction products from the consummation of the acquisition in November 2009 to year end. See Part II, Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations IDC Acquisition, above.

Higher Education Institution Revenue

The increase in higher education institution revenue was primarily due to an increase of 33.1% in card fees and an increase of 55.3% in transaction fees related to our OneDisburse® product due primarily to an increase in the number of higher education institutional clients using this product compared to the previous year. The inclusion of 42 days of revenue generated by the payment transaction products and services that we acquired when we purchased IDC in November 2009 also accounted for 33.7% of the total increase in higher education institution revenue.

Other Revenue

The decrease in other revenue was primarily due to a decrease of 83.5% in the processing fees that our bank partner pays to us caused by a decline in prevailing interest rates during the year ended December 31, 2009. This decrease was partially offset by an increase of 64.4% in the marketing incentive fees that MasterCard paid to us.

Cost of Revenue

The increase in cost of revenue was comprised of an increase of $2.8 million, or 184.4%, in interchange expenses, an increase of $1.7 million, or 32.5%, in data processing expenses, an increase of $1.2 million, or 24.3%, in uncollectible fees and write-offs, an increase of $1.8 million, or 84.6%, in customer service expenses and an increase of $0.6 million, or 33.3%, in card issuance expenses. The growth in these expenses was primarily due to an increase of 81.2% in the number of active OneAccounts and the related increase in transaction volume for our banking services. The inclusion of 42 days of costs related to our recently acquired payment transaction products and services accounted for $1.4 million, or 17.1%, of the total increase in cost of revenue.

General and Administrative Expense

The increase in general and administrative expense was primarily due to an increase of $1.7 million, or 28.8%, in employee compensation and an increase of $0.8 million, or 210.7%, in fees for professional services during the year ended December 31, 2009, which increased in part as a result of the inclusion of 42 days of expenses related to our recently acquired payment transaction products and services, as well as an increase of $0.9 million, or 178.5%, in stock-based compensation.

Product Development Expense

The increase in product development expense was primarily due to an increase of $0.7 million, or 40.4%, in costs related to employee compensation allocated to product development expense during the year ended December 31, 2009.

Sales and Marketing Expense

The increase in sales and marketing expense was primarily due to an increase of $1.9 million, or 82.5%, in costs related to employee compensation allocated to sales and marketing expense and an increase of $1.1 million, or 92.4%, in the non-cash expense related to the vesting of certain shares held by Kevin Jones during the year ended December 31, 2009.

Income Tax Expense

The increase in income tax expense was primarily due to an increase of $12.2 million, or 123.1%, in net income before taxes. The effective tax rates for the years ended December 31, 2008 and 2009 were 35.7% and 35.8%, respectively.

Liquidity and Capital Resources

Sources of Liquidity

Our primary sources of liquidity are cash flows from operations and borrowings under our Credit Facility. As of December 31, 2010, we had $34.5 million in cash and cash equivalents, $14.7 million in available-for-sale securities and $50 million available under our Credit Facility. Our primary liquidity requirements are for working capital, capital expenditures, including our planned real estate development project, product development expenses and general corporate needs. As of December 31, 2010, we had working capital of $39.7 million.

During 2010, we issued common stock for net proceeds of $37.2 million. We used $10.0 million of the net proceeds to repay amounts then outstanding under our prior credit facility and deposited $8.25 million into escrow to satisfy our post-closing obligations under the IDC stock purchase agreement. The remaining amount of net proceeds remains available for our strategic objectives and for general corporate

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purposes.

Senior Secured Revolving Credit Facility

Higher One, Inc. entered into a senior secured revolving credit facility dated as of August 26, 2008 that was subsequently amended as of July 15, 2009 and November 19, 2009. We refer to the credit facility, as amended, as the Prior Credit Facility. The Prior Credit Facility matured on December 31, 2010 and there were no amounts outstanding at maturity.

On December 31, 2010, we entered into a new senior secured revolving credit facility, or our Credit Facility. Among other things, the Credit Facility increased the maximum amount available to be drawn to $50 million and allows us to request an increase in this limit to $100 million. Any amounts drawn under the amended and restated credit facility are payable in a single maturity on December 31, 2013. Each of Higher One Holdings, Inc., Higher One Machines, Inc., Higher One Payments, Inc., Higher One Real Estate, Inc. and Higher One Real Estate SP, LLC, which we refer to collectively, together with Higher One Inc., as the Credit Facility Loan Obligors, is a guarantor of Higher One, Inc. s obligations under the Credit Facility.

The Credit Facility is secured by a perfected first priority security interest in all of the capital stock of Higher One, Inc. and its subsidiaries, and substantially all of each Credit Facility Loan Obligor s tangible and intangible assets, other than intellectual property. Each of the Credit Facility Loan Obligors has also granted to the administrative agent under the Credit Facility a negative pledge of the intellectual property of Higher One, Inc. and its subsidiaries, including patents and trademarks that are pending and acquired in the future.

At our option, each advance under the Credit Facility accrues interest on the basis of a base rate or on the basis of a one-month, two-month or three-month Eurodollar rate, plus in either case, the applicable margin based on our funded debt to EBITDA ratio, at the time each loan is made. We also pay commitment fees for the unused portion of the revolving loan on a quarterly basis equal to the product obtained by multiplying the applicable margin for commitment fees by the average daily unused commitment for that calendar quarter. The applicable margin for base rate advances is between (1.25%) and 0%, subject to a minimum rate of 2%, and the applicable margin for Eurodollar rate advances is between 2.0% and 3.25%. The applicable margin for commitment fees is between 0.25% and 0.375%. The base rate is the higher of Bank of America s announced prime rate, the federal funds rate plus 0.50% or the Eurodollar rate plus 1.00%. Interest on Eurodollar loans is payable at the end of each applicable interest period. Interest on base rate advances is payable quarterly in arrears.

The Credit Facility contains certain affirmative covenants including, among other things, covenants to furnish the lenders with financial statements and other financial information and to provide the lenders notice of material events and information regarding collateral. The Credit Facility also contains certain negative covenants that, among other things, restrict Higher One, Inc. s ability, subject to certain exceptions, to incur additional indebtedness, grant liens on its assets, undergo fundamental changes, make investments, sell assets, make restricted payments, change the nature of its business and engage in transactions with its affiliates.

In addition, the Credit Facility contains certain financial covenants that require we maintain a minimum EBITDA level measured on the prior four fiscal quarters of $50 million, a funded debt to EBITDA ratio not to exceed 2.00 to 1.00 and a fixed charge coverage ratio of at least 1.25 to 1.00. We are in compliance with all of the relevant covenants as of December 31, 2010.

Cash Flows

The following table presents information regarding our cash flows, cash and cash equivalents for the years ended December 31, 2008, 2009 and 2010:

	2008	Year Ended December 31, 2009 (in thousands)	2010
Net cash provided by (used for)			
Operating activities	$ 9,962	$ 20,656	$ 40,056
Investing activities	(3,340)	(18,731)	(31,756)
Financing activities	(14,889)	(74)	22,845
Increase (decrease) in cash and cash equivalents	$ (8,267)	$ 1,851	$ 31,145
Cash and cash equivalents, end of period	$ 1,488	$ 3,339	$ 34,484

Operating Activities

The $19.4 million increase in net cash provided by operating activities for the year ended December 31, 2010 was primarily comprised of an increase of $10.8 million in net income and an $8.6 million increase in adjustments to reconcile net income to net cash, including a $4.9 million increase in stock-based sales acquisition expense and $4.3 million in depreciation and amortization. The increase in stock-based sales acquisition expense is due primarily to higher average share price at the date of vesting.

The $10.7 million increase in net cash provided by operating activities from 2008 to 2009 was primarily comprised of an increase of $7.8 million in net income, an increase of $1.5 million in depreciation and amortization, a decrease of $1.6 million in income receivable, an increase of $1.1 million in stock-based customer acquisition expense and an increase of $0.9 million in stock-based compensation, which were partially offset by a deferred income tax benefit of $0.8 million in 2009 compared to a deferred income tax expense of $1.8 million in 2008. The increase in depreciation and amortization was primarily attributable to increased tangible and intangible asset purchases and increased deferred implementation costs; the decrease in income receivable was attributable to an increase in our receipt of cash owed to us; the increase in stock-based customer acquisition expense was primarily attributable to increased vesting of certain shares acquired by Kevin Jones in connection with our acquisition of EduCard in 2008; and the increase in stock-based compensation was primarily attributable to an increase in the fair value of options granted and additional grants of options. The income tax benefit in 2009 was primarily the result of the increased vesting of certain shares acquired by Kevin Jones described above.

Investing Activities

Net cash used for investing activities for 2010 primarily related to our investment in available for sale securities, the payment and deposit into escrow related to our acquisition of IDC and our purchases of fixed assets. Net cash used for investing activities for 2009 primarily related to our acquisition of CASHNet in November 2009, as well as our purchase of fixed assets, including computers, software and ATM equipment. Net cash used for investing activities for 2008 primarily related to our acquisition of EduCard in June 2008, as well as our purchase of fixed assets, net of disposals, including computers, software and ATM equipment.

We believe that our cash flow from operations together with our existing liquidity sources will be sufficient to fund our operations and anticipated capital expenditures over at least the next 12 months.

Real Estate Development Project

As of December 31, 2010, we have incurred approximately $2.5 million on a project to develop two existing commercial buildings located in New Haven, Connecticut into which we expect to move at the completion of the project in 2012. We anticipate making additional payments in 2011 and 2012 as progress continues on the project. The project has a total estimated cost of approximately $47 million. Our net cost will be reduced by federal and state subsidies and tax credits from various programs and entities described below. In connection with the project, we formed two new subsidiaries, Higher One Real Estate, Inc., or Real Estate Inc., and Higher One Real Estate SP, LLC, or Real Estate LLC.

On November 9, 2010, Real Estate LLC entered into an agreement with Winchester Arms NH, LLC to develop the buildings.

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Real Estate LLC signed a construction contract with John Moriarty & Associates, or Moriarty, effective January 28, 2011, whereby Moriarty will be the general contractor for the project.

On February 18, 2011, Real Estate LLC signed a land lease with Science Park Development Corporation, or SPDC, which owns the property on which the two buildings reside, concerning the leasing, expansion and buyout of the land. The agreement provides for a long term lease of the land at a nominal cost per year and includes a buyout option for a nominal amount after seven years.

We intend to fund this development project using existing cash and additional cash generated from operations.

A summary of the subsidies, grants and credits we expect to receive are as follows:

Name of program	Estimated amount (in millions)	Nature of the program	Status
State of Connecticut Department of Economic and Community Development, or DECD, Urban and Industrial Site Reinvestment Tax Credits	$ 18.5	State tax credits beginning in 2013 and continuing through 2019	All necessary approvals have been obtained.
Federal Historic Preservation Tax Incentives Program	$ 6.0	Federal tax credit equal to 20% of qualified rehabilitation expenditures related to the project.	All necessary approvals have been obtained, we will be eligible to receive the credits when the building is placed in service.
DECD Urban Act Grant	$ 3.5	Grant that will reduce our real estate development costs	Grant will be voted on at a future meeting of the State of Connecticut Bond Commission
DECD Environmental Remediation Grant	$ 2.0	Grant that will reduce our net environmental remediation costs	Bond commission approval has been obtained.
Connecticut Development Authority Sales and Use Tax Relief Program	$ 1.0	Provides relief of our obligation to pay Connecticut sales and use tax on tangible property acquired in connection with the project up to $1.0 million	All necessary approvals have been obtained.
Other contributions	$ 4.3	Cash contributions from (i) SPDC upon our completion of the project; (ii) prior building owner to offset a portion our environmental remediation costs; and (iii) SPDC based on the value of state historic tax credits awarded to SPDC.	All necessary approvals have been obtained.
New Market Tax Credit	$ 2.0	Federal credit program that permits taxpayers to receive a credit against federal income taxes for making qualified equity investments in designated Community Development Entities, or CDE.	We are in the process of identifying a CDE that we will partner with to obtain financing for the project.

Many of these programs have criteria that we must meet in order to receive the subsidies, grants and credits and also criteria that we must meet on an ongoing basis, such as a minimum employment threshold, in order to prevent forfeiture of the subsidies, grants and credits, and in some cases the imposition of a penalty. Higher One Holdings, Inc. has provided a limited guaranty of Higher One, Inc. s obligations with respect to the Urban and Industrial Site Reinvestment Tax Credits described in the table above.

Financing Activities

The net cash provided by financing activities in 2010 was primarily related to proceeds received from our initial public offering, net of issuance costs, of $37.2 million, a tax benefit related to options of $2.8 million and proceeds received from the exercise of stock options of $1.0 million. These were partially offset by net payments of $18.0 million of debt under our Prior Credit Facility. Net cash used in financing activities for

2009 primarily related to repayments under our Prior Credit Facility, partially offset by proceeds from the issuance of debt and from notes payable relating to borrowings under the Prior Credit

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Facility. Net cash used in financing activities for 2008 primarily related to the completion of our tender offer to purchase certain outstanding capital stock in August 2008, which was partially offset by the proceeds from our sale of preferred stock in August 2008 and borrowings under our Prior Credit Facility.

Supplemental Non-GAAP Financial and Operating Information

		Year Ended December 31,	
	2008	2009	2010
		(in thousands)	
Adjusted EBITDA(1)	$ 13,140	$ 30,516	$ 59,465
Adjusted net income(2)	$ 7,725	$ 18,085	$ 34,418
Number of students enrolled at OneDisburse® client higher education institutions at end of period	1,605	2,331	3,281
Number of students enrolled at payment transaction client higher education institutions at end of period	29	1,949	2,460
Number of OneAccounts at end of period	554	1,004	1,618

We define adjusted EBITDA as net income before interest, taxes and depreciation and amortization, or EBITDA, further adjusted to remove the effects of stock-based customer acquisition expense related to our grants of common stock in connection with our acquisition of EduCard in 2008 and cash-based customer acquisition expense related to the acquisition of IDC, stock-based compensation expense and a non-recurring milestone bonus paid to non-executive employees in 2009 upon our reaching a particular long-term operational target. Neither EBITDA nor adjusted EBITDA should be considered as an alternative to net income, operating income or any other measure of financial performance calculated and presented in accordance with GAAP. Our EBITDA and adjusted EBITDA may not be comparable to similarly titled measures of other organizations because other organizations may not calculate EBITDA and adjusted EBITDA in the same manner as we do. We prepare and present adjusted EBITDA to eliminate the effect of items that we do not consider indicative of our core operating performance. You are encouraged to evaluate our adjustments and the reasons we consider them appropriate.

We believe adjusted EBITDA is useful to our board of directors, management and investors in evaluating our operating performance for the following reasons:

adjusted EBITDA is widely used by investors to measure a company s operating performance without regard to certain items, such as interest expense, income tax expense, depreciation and amortization, stock-based expenses and certain non-recurring items, that can vary substantially from company to company and from period to period depending upon their financing and accounting methods, the book value of their assets, their capital structures and the method by which their assets were acquired;

securities analysts use adjusted EBITDA as a supplemental measure to evaluate the overall operating performance of companies;

because non-cash equity grants made at a certain price and point in time do not necessarily reflect how our business is performing at any particular time, stock-based customer acquisition expense and stock-based compensation expense are not key measures of our core operating performance;

because cash-based customer acquisition expense is a non-recurring item related to the acquisition of IDC and does not reflect how our business is performing at any particular time, cash-based customer acquisition expense is therefore not key measure of our core operating performance; and

because the milestone bonus was a non-recurring expense that we recorded upon reaching a particular long-term operational target that we do not expect to incur again in the near-term, the milestone bonus does not necessarily reflect how our business is

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performing at any particular time and is therefore not a key measure of our core operating performance.

(1) The following table presents a reconciliation of net income, the most comparable GAAP measure, to EBITDA and adjusted EBITDA for each of the periods indicated:

	Year Ended December 31,		
	2008	2009	2010
	(in thousands)		
Net income	$ 6,378	$ 14,219	$ 25,059
Interest income	(152)	(4)	(29)
Interest expense	357	558	729
Income tax expense	3,547	7,925	15,488
Depreciation and amortization	1,452	2,969	7,292
EBITDA	11,582	25,667	48,539
Other income	(234)	(17)	
Warrant fair value adjustment	55		
Stock-based and other customer acquisition expense	1,239	2,385	8,013
Stock-based compensation expense	498	1,387	2,913
Milestone bonus		1,094	
Adjusted EBITDA	$ 13,140	$ 30,516	$ 59,465

We define adjusted net income as net income, adjusted to eliminate (a) stock-based compensation expense related to incentive stock option grants and (b) after giving effect to tax adjustments, stock-based compensation expense related to non-qualified stock option grants, stock-based customer acquisition expense related to our grant of common stock in connection with our acquisition of EduCard in 2008, cash-based customer acquisition expense related to the acquisition of IDC, a non-recurring milestone bonus paid to non-executive employees in 2009 upon our reaching a particular long-term operational target and amortization expenses related to intangible assets and financing costs. Adjusted net income should not be considered as an alternative to net income, operating income or any other measure of financial performance calculated and presented in accordance with GAAP. Our adjusted net income may not be comparable to similarly titled measures of other organizations because other organizations may not calculate adjusted net income in the same manner as we do. We prepare adjusted net income to eliminate the effect of items that we do not consider indicative of our core operating performance. You are encouraged to evaluate our adjustments and the reasons we consider them appropriate.

We believe adjusted net income is useful to our board of directors, management and investors in evaluating our operating performance for the following reasons:

because non-cash equity grants made at a certain price and point in time do not necessarily reflect how our business is performing at any particular time, stock-based customer acquisition expense and stock-based compensation expense are not key measures of our core operating performance;

because cash-based customer acquisition expense is a non-recurring item related to the acquisition of IDC and does not reflect how our business is performing at any particular time, cash-based customer acquisition expense is therefore not key measure of our core operating performance;

because the milestone bonus was a non-recurring expense that we recorded upon reaching a particular long-term operational target that we do not expect to incur again in the near-term, the milestone bonus does not necessarily reflect how our business is performing at any particular

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time and is therefore not a key measure of our core operating performance; and

amortization expenses can vary substantially from company to company and from period to period depending upon their financing and accounting methods, the fair value and average expected life of their acquired intangible assets, their capital structures and the method by which their assets were acquired.

(2) The following table presents a reconciliation of net income, the most comparable GAAP measure, to adjusted net income for each of the periods indicated:

	Year Ended December 31,		
	2008	2009	2010
	(in thousands)		
Net income	$ 6,378	$ 14,219	$ 25,059
Stock-based and other customer acquisition expense	1,239	2,385	8,013
Stock-based compensation expense - ISO	312	610	1,526
Stock-based compensation expense - NQO	186	777	1,387
Milestone bonus expense		1,094	
Amortization of intangibles	153	710	3,070
Amortization of finance costs	31	113	204
Total pre-tax adjustments	1,921	5,689	14,200
Tax rate	35.7%	35.9%	38.2%
Tax adjustment(1)	574	1,823	4,841
Adjusted net income	$ 7,725	$ 18,085	$ 34,418

(1) We have tax effected all the pre-tax adjustments except for stock-based compensation expense for incentive stock options, which are generally not tax deductible.

The adjusted EBITDA and adjusted net income measures presented in this annual report on Form 10-K may not be comparable to similarly titled measures presented by other companies, and may not be identical to corresponding measures used in our various agreements, in particular our credit facility agreement.

Contractual Obligations

The following table summarizes our contractual obligations as of December 31, 2010 and the effect such obligations are expected to have on our liquidity and cash flows in future periods.

	Payments Due by Period					
	Total	Less Than 1 Year	1 to 3 Years	3 to 5 Years	5+ Years	All Other
	(in thousands)					
Operating lease obligations(1)	$ 1,600	$ 843	$ 366	$ 375	$ 16	$

Purchase obligations(2)	14,320	3,780	8,432	2,108		
Uncertain tax positions and related interest(3)	684					684
Total contractual obligations	$ 16,604	$ 4,623	$ 8,798	$ 2,483	$ 16	$ 684

(1) We lease certain property in New Haven, Connecticut and Oakland, California under non-cancelable

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operating leases. The lease in New Haven is currently due to expire on July 31, 2011 and the lease in Oakland is due to expire on January 31, 2016.

(2) Purchase obligations include minimum amounts committed under contracts for services.

(3) We are unable to reasonably estimate the timing of such liability and interest payments in individual years beyond 12 months due to uncertainties in the timing of the effective settlement of tax positions.

Off-Balance Sheet Arrangements

We are not a party to any off-balance sheet arrangements.

Recent Accounting Pronouncements

We review new accounting standards to determine the expected financial impact, if any, that the adoption of each such standard will have. As of the filing of this report, there were no new accounting standards issued that we expect to have a material impact on our consolidated financial position, results of operations or liquidity.

In October 2009, the FASB issued Accounting Standards Update, or ASU, No. 2009-13 *Multiple-Deliverable Revenue Arrangements*. This ASU establishes the accounting and reporting guidance for arrangements including multiple revenue-generating activities. This ASU provides amendments to the criteria for separating deliverables, measuring and allocating arrangement consideration to one or more units of accounting. The amendments in this ASU also establish a selling price hierarchy for determining the selling price of a deliverable. Significantly enhanced disclosures are also required to provide information about a vendor s multiple-deliverable revenue arrangements, including information about the nature and terms, significant deliverables and its performance within arrangements. The amendments also required providing information about the significant judgments made and changes to those judgments and about how the application of the relative selling-price method affects the timing or amount of revenue recognition. The amendments in this ASU are effective prospectively for revenue arrangements entered into or materially modified in the fiscal years beginning on or after June 15, 2010. We will adopt this standard on January 1, 2011 and do not expect the standard to have a material impact on our results of operations, cash flows or financial position.

In October 2009, the FASB issued ASU No. 2009-14, *Certain Revenue Arrangements That Include Software Elements.* This ASU changes the accounting model for revenue arrangements that include both tangible products and software elements that are essential to the functionality, and scopes these products out of current software revenue guidance. The new guidance will include factors to help companies determine what software elements are considered essential to the functionality. The amendments will now subject software-enabled products to other revenue guidance and disclosure requirements, such as guidance surrounding revenue arrangements with multiple-deliverables. The amendments in this ASU are effective prospectively for revenue arrangements entered into or materially modified in the fiscal years beginning on or after June 15, 2010. We will adopt this standard on January 1, 2011 and do not expect the standard to have a material impact on our results of operations, cash flows or financial position.

In April 2010, the FASB issued ASU No. 2010-17, *Milestone Method of Revenue Recognition,* which indicates the criteria that should be met for determining whether the milestone method of revenue recognition is appropriate. Companies can recognize consideration that is contingent upon achievement of a milestone in its entirety as revenue in the period in which the milestone is achieved only if the milestone meets all criteria to be considered substantive. This ASU is effective for fiscal years beginning after June 15, 2010. We will adopt this standard on January 1, 2011 and do not expect the standard to have a material impact on our results of operations, cash flows or financial position.

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Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Our principal market risk relates to interest rate sensitivity, which is the risk that future changes in interest rates will reduce our net income or net assets. Our Credit Facility accrues interest at a rate equal to a base rate or Eurodollar rate plus an applicable margin (depending on Higher One, Inc. s funded debt to EBITDA ratio). Based upon a sensitivity analysis at January 1, 2011, assuming average outstanding borrowings during the year ended December 31, 2011 of $10.0 million, a hypothetical 50 basis point increase in interest rates would result in an increase in interest expense of $0.05 million.

In addition, we receive processing fees paid from our bank partner, based on prevailing interest rates and the total deposits held in our OneAccounts. Since 2008, fees paid by our bank partner have been relatively small because of depressed interest rates. A change in interest rates would affect the amount of processing fees that we earn and therefore would have an effect on our revenue, cash flows and results of operations.

Item 8. Financial Statements and Supplementary Data

Information required by this item is contained in our consolidated financial statements, related footnotes and the report of PricewaterhouseCoopers LLP, which information follows the signature page to this annual report and is incorporated herein by reference.

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

None.

Item 9A(T). Controls and Procedures

Disclosure Controls and Procedures

Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures as of December 31, 2010. The term disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the rules and forms of the SEC. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives, and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of December 31, 2010, our chief executive officer and chief financial officer concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

Management Report on Internal Control Over Financial Reporting

This annual report does not include a report of management s assessment regarding internal control over financial reporting or an attestation report of the company s registered public accounting firm due to a transition period established by rules of the SEC for newly public companies.

Changes in Internal Control Over Financial Reporting

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During the quarter ended December 31, 2010, we remediated our previously identified material weakness by, among other things, expanding our current finance and accounting staff, formalizing our accounting policies and internal controls documentation and strengthening supervisory reviews by our management. These changes have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act).

Item 9B. Other Information

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance

Executive Officers and Directors

The following table sets forth information about individuals who currently serve as our executive officers and/or directors.

Name	Age	Title
Dean Hatton	50	President, Chief Executive Officer and Director
Mark Volchek		