

ITT EDUCATIONAL SERVICES INC  
Form 10-Q  
April 22, 2010

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2010  
OR

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

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

Commission file number 1-13144

ITT EDUCATIONAL SERVICES, INC.  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

36-2061311  
(I.R.S. Employer Identification  
No.)

13000 North Meridian Street  
Carmel, Indiana  
(Address of principal executive  
offices)

46032-1404  
(Zip Code)

Registrant's telephone number, including area code: (317)  
706-9200

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

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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  (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

34,537,809

Number of  
shares of  
Common  
Stock, \$.01 par  
value,  
outstanding at  
March 31, 2010

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ITT EDUCATIONAL SERVICES, INC.  
Carmel, Indiana

Quarterly Report to Securities and Exchange Commission  
March 31, 2010

PART I  
FINANCIAL INFORMATION

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ITT EDUCATIONAL SERVICES, INC.  
CONDENSED CONSOLIDATED BALANCE SHEETS  
(Dollars in thousands, except per share data)

|   | March 31, 2010<br>(unaudited) | As of<br>December 31,<br>2009 | March 31, 2009<br>(unaudited) |
|---|-------------------------------|-------------------------------|-------------------------------|
| <b>Assets</b>   |                               |                               |                               |
| <b>Current assets:</b>  |                               |                               |                               |
| Cash and cash equivalents   | \$ 165,544                    | \$ 128,788                    | \$ 219,642                    |
| Short-term investments  | 156,143                       | 143,407                       | 146,062                       |
| Restricted cash   | 5,298                         | 1,891                         | 11                            |
| Accounts receivable, net  | 88,290                        | 85,426                        | 51,513                        |
| Deferred income taxes   | 13,321                        | 13,799                        | 12,143                        |
| Prepaid expenses and other current assets   | 19,735                        | 17,651                        | 15,960                        |
| <b>Total current assets</b>   | <b>448,331</b>                | <b>390,962</b>                | <b>445,331</b>                |
| Property and equipment, net   | 191,438                       | 195,449                       | 166,582                       |
| Deferred income taxes   | 9,720                         | 6,416                         | 8,887                         |
| Other assets  | 27,900                        | 23,878                        | 3,682                         |
| <b>Total assets</b>   | <b>\$ 677,389</b>             | <b>\$ 616,705</b>             | <b>\$ 624,482</b>             |
| <b>Liabilities and Shareholders' Equity</b>   |                               |                               |                               |
| <b>Current liabilities:</b>   |                               |                               |                               |
| Accounts payable  | \$ 68,474                     | \$ 61,275                     | \$ 63,658                     |
| Accrued compensation and benefits   | 17,465                        | 26,323                        | 23,670                        |
| Accrued income taxes  | 49,702                        | 10,218                        | 36,959                        |
| Other accrued liabilities   | 16,149                        | 15,043                        | 11,896                        |
| Deferred revenue  | 191,795                       | 171,933                       | 133,137                       |
| <b>Total current liabilities</b>  | <b>343,585</b>                | <b>284,792</b>                | <b>269,320</b>                |
| Long-term debt  | 150,000                       | 150,000                       | 150,000                       |
| Other liabilities   | 28,294                        | 25,328                        | 20,810                        |
| <b>Total liabilities</b>  | <b>521,879</b>                | <b>460,120</b>                | <b>440,130</b>                |
| <b>Shareholders' equity:</b>  |                               |                               |                               |
| Preferred stock, \$.01 par value,<br>5,000,000 shares authorized, none<br>issued      | --                            | --                            | --                            |
| Common stock, \$.01 par value,<br>300,000,000<br>shares authorized, 54,068,904 issued | 541                           | 541                           | 541                           |
| Capital surplus   | 160,371                       | 154,495                       | 144,004                       |
| Retained earnings   | 1,090,413                     | 1,006,903                     | 771,666                       |
| Accumulated other comprehensive<br>(loss)   | (9,851 )                      | (10,093 )                     | (13,293 )                     |

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|   |              |            |            |
|---|--------------|------------|------------|
| Treasury stock, 19,531,095,<br>18,622,809     |              |            |            |
| and 15,743,252 shares, at cost                | (1,085,964 ) | (995,261 ) | (718,566 ) |
| Total shareholders' equity                    | 155,510      | 156,585    | 184,352    |
| Total liabilities and shareholders'<br>equity | \$ 677,389   | \$ 616,705 | \$ 624,482 |

The accompanying notes are an integral part of these condensed consolidated financial statements.

ITT EDUCATIONAL SERVICES, INC.  
CONDENSED CONSOLIDATED STATEMENTS OF INCOME  
(Dollars and shares in thousands, except per share data)  
(unaudited)

|  | Three Months Ended<br>March 31, |            |
|--|---------------------------------|------------|
|  | 2010                            | 2009       |
| Revenue                                      | \$ 383,957                      | \$ 288,033 |
| Costs and expenses:                          |                                 |            |
| Cost of educational services                 | 134,382                         | 101,087    |
| Student services and administrative expenses | 106,960                         | 88,459     |
| Total costs and expenses                     | 241,342                         | 189,546    |
| Operating income                             | 142,615                         | 98,487     |
| Interest income                              | 709                             | 1,233      |
| Interest (expense)                           | (420 )                          | (194 )     |
| Income before provision for income taxes     | 142,904                         | 99,526     |
| Provision for income taxes                   | 55,453                          | 38,608     |
| Net income                                   | \$ 87,451                       | \$ 60,918  |
| Earnings per share:                          |                                 |            |
| Basic  | \$ 2.50                         | \$ 1.58    |
| Diluted                                      | \$ 2.46                         | \$ 1.56    |
| Weighted average shares outstanding:         |                                 |            |
| Basic  | 35,028                          | 38,558     |
| Diluted                                      | 35,499                          | 39,062     |

The accompanying notes are an integral part of these condensed consolidated financial statements.

ITT EDUCATIONAL SERVICES, INC.  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Dollars in thousands)  
(unaudited)

|  | Three Months Ended<br>March 31, |           |
|--|---------------------------------|-----------|
|  | 2010                            | 2009      |
| Cash flows from operating activities:  |                                 |           |
| Net income   | \$ 87,451                       | \$ 60,918 |
| Adjustments to reconcile net income to net cash flows from operating activities: |                                 |           |
| Depreciation and amortization  | 6,758                           | 5,772     |
| Provision for doubtful accounts  | 22,765                          | 14,209    |
| Deferred income taxes  | (2,978 )                        | (1,689 )  |
| Excess tax benefit from stock option exercises                                   | (921 )                          | (3,793 )  |
| Stock-based compensation expense   | 4,813                           | 4,183     |
| Other  | 156                             | 135       |
| Changes in operating assets and liabilities:                                     |                                 |           |
| Restricted cash  | (3,407 )                        | 10,132    |
| Accounts receivable  | (25,629 )                       | (35,943 ) |
| Accounts payable   | 7,199                           | 8,843     |
| Accrued income taxes   | 40,546                          | 26,149    |
| Other operating assets and liabilities   | 2,505                           | 1,481     |
| Deferred revenue   | 19,862                          | (29,069 ) |
| Net cash flows from operating activities   | 159,120                         | 61,328    |
| Cash flows from investing activities:  |                                 |           |
| Facility expenditures and land purchases   | (839 )                          | (1,074 )  |
| Capital expenditures, net  | (5,298 )                        | (4,608 )  |
| Proceeds from sales and maturities of investments and notes                      | 84,698                          | 48,598    |
| Purchase of investments and notes  | (107,172 )                      | (55,770 ) |
| Net cash flows from investing activities   | (28,611 )                       | (12,854 ) |
| Cash flows from financing activities:  |                                 |           |
| Excess tax benefit from stock option exercises                                   | 921                             | 3,793     |
| Proceeds from exercise of stock options  | 1,026                           | 5,823     |
| Repurchase of common stock and shares tendered for taxes                         | (95,700 )                       | (64,703 ) |
| Net cash flows from financing activities   | (93,753 )                       | (55,087 ) |
| Net change in cash and cash equivalents  | 36,756                          | (6,613 )  |
| Cash and cash equivalents at beginning of period                                 | 128,788                         | 226,255   |

|  |    |         |    |         |
|--|----|---------|----|---------|
| Cash and cash equivalents at end of period | \$ | 165,544 | \$ | 219,642 |
|--|----|---------|----|---------|

The accompanying notes are an integral part of these condensed consolidated financial statements.

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ITT EDUCATIONAL SERVICES, INC.  
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY  
(Dollars and shares in thousands)

|  | Common Stock<br>Shares | Common Stock<br>Amount | Capital<br>Surplus | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Income/(Loss) | Common Stock in<br>Treasury<br>Shares | Common Stock in<br>Treasury<br>Amount | Total     |
|--|------------------------|------------------------|--------------------|----------------------|--|---------------------------------------|---------------------------------------|-----------|
| Balance as of<br>December 31,<br>2008  | 54,069                 | \$541                  | \$135,655          | \$718,100            | \$ (13,384 )   | (15,352)                              | \$(667,068 )                          | \$173,844 |
| For the three<br>months ended<br>March 31, 2009<br>(unaudited):                    |                        |                        |                    |                      |  |                                       |                                       |           |
| Net income   |                        |                        |                    | 60,918               |  |                                       |                                       | 60,918    |
| Other<br>comprehensive<br>income   |                        |                        |                    |                      |  |                                       |                                       |           |
| Amortization of<br>prior service cost,<br>net of \$3 of<br>income tax              |                        |                        |                    |                      | 4  |                                       |                                       | 4         |
| Amortization of<br>net actuarial<br>pension loss, net of<br>\$222 of income<br>tax |                        |                        |                    |                      | 344  |                                       |                                       | 344       |
| Unrealized (loss)<br>Comprehensive<br>income                                       |                        |                        |                    |                      | (257 )   |                                       |                                       | (257 )    |
| Exercise of stock<br>options and equity<br>awards                                  |                        |                        |                    | (7,354 )             |  | 139                                   | 13,177                                | 5,823     |
| Tax benefit from<br>exercise of stock<br>options and equity<br>award vesting       |                        |                        | 4,166              |                      |  |                                       |                                       | 4,166     |
| Stock-based<br>compensation  |                        |                        | 4,183              |                      |  |                                       |                                       | 4,183     |
| Common shares<br>repurchased   |                        |                        |                    |                      |  | (528 )                                | (64,360 )                             | (64,360 ) |
| Issuance of shares<br>for Directors'<br>compensation                               |                        |                        | 2                  |                      |  | 1                                     | 28                                    | 30        |
| Shares tendered<br>for taxes   |                        |                        |                    |                      |  | (3 )                                  | (343 )                                | (343 )    |
| Balance as of<br>March 31, 2009  | 54,069                 | 541                    | 144,004            | 771,666              | (13,293 )  | (15,743)                              | (718,566 )                            | 184,352   |

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For the nine  
months ended  
December 31,  
2009 (unaudited):

|  |        |       |         |           |           |           |            |  |            |
|--|--------|-------|---------|-----------|-----------|-----------|------------|--|------------|
| Net income   |        |       |         |           | 239,345   |           |            |  | 239,345    |
| Other comprehensive income:  |        |       |         |           |           |           |            |  |            |
| Amortization of prior service cost, net of \$8 of income tax             |        |       |         |           | 13        |           |            |  | 13         |
| Amortization of net actuarial pension loss, net of \$2,164 of income tax |        |       |         |           | 3,353     |           |            |  | 3,353      |
| Pension settlement loss, net of \$18 of income tax                       |        |       |         |           | 28        |           |            |  | 28         |
| Unrealized (loss)  |        |       |         |           | (194 )    |           |            |  | (194 )     |
| Comprehensive income   |        |       |         |           |           |           |            |  | 242,545    |
| Exercise of stock options and equity awards                              |        |       |         |           | (4,108 )  | 71        | 7,085      |  | 2,977      |
| Tax benefit from exercise of stock options and equity award vesting      |        | 1,600 |         |           |           |           |            |  | 1,600      |
| Stock-based compensation   |        | 8,891 |         |           |           |           |            |  | 8,891      |
| Common shares repurchased  |        |       |         |           |           | (2,950 )  | (283,763 ) |  | (283,763 ) |
| Shares tendered for taxes  |        |       |         |           |           | (1 )      | (17 )      |  | (17 )      |
| Balance as of December 31, 2009  | 54,069 | 541   | 154,495 | 1,006,903 | (10,093 ) | (18,623 ) | (995,261 ) |  | 156,585    |

For the three  
months ended  
March 31, 2010  
(unaudited):

|   |  |  |  |  |        |  |  |  |        |
|---|--|--|--|--|--------|--|--|--|--------|
| Net income  |  |  |  |  | 87,451 |  |  |  | 87,451 |
| Other comprehensive income:                       |  |  |  |  |        |  |  |  |        |
| Amortization of prior service cost, net of \$3 of |  |  |  |  | 4      |  |  |  | 4      |

|  |        |       |           |             |             |           |               |           |
|--|--------|-------|-----------|-------------|-------------|-----------|---------------|-----------|
| income tax   |        |       |           |             |             |           |               |           |
| Amortization of net actuarial pension loss, net of \$147 of income tax |        |       |           |             | 230         |           |               | 230       |
| Unrealized gain  |        |       |           |             | 8           |           |               | 8         |
| Comprehensive income   |        |       |           |             |             |           |               | 87,693    |
| Exercise of stock options and equity awards                            |        |       | (3,942 )  |             | 51          | 4,968     |               | 1,026     |
| Tax benefit from exercise of stock options and equity award vesting    | 1,063  |       |           |             |             |           |               | 1,063     |
| Stock-based compensation   | 4,813  |       |           |             |             |           |               | 4,813     |
| Common shares repurchased  |        |       |           |             | (953 )      | (95,025 ) |               | (95,025 ) |
| Issuance of shares for Directors' compensation                         |        |       | 1         |             | 1           | 29        |               | 30        |
| Shares tendered for taxes  |        |       |           |             | (7 )        | (675 )    |               | (675 )    |
| Balance as of March 31, 2010   | 54,069 | \$541 | \$160,371 | \$1,090,413 | \$ (9,851 ) | (19,531)  | \$(1,085,964) | \$155,510 |

The accompanying notes are an integral part of these condensed consolidated financial statements.

ITT EDUCATIONAL SERVICES, INC.  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
March 31, 2010  
(Dollars in thousands, except per share data and unless otherwise stated)

1. The Company and Basis of Presentation

We are a leading provider of technology-oriented postsecondary education in the United States based on revenue and student enrollment. As of March 31, 2010, we were offering master, bachelor and associate degree programs to more than 84,000 students at ITT Technical Institute and Daniel Webster College locations. As of March 31, 2010, we had 127 locations (including 123 campuses and four learning sites) in 38 states. All of our locations are authorized by the applicable education authorities of the states in which they operate and are accredited by an accrediting commission recognized by the U.S. Department of Education ("ED"). We have provided career-oriented education programs since 1969 under the "ITT Technical Institute" name and since June 2009 under the "Daniel Webster College" name. Our corporate headquarters are located in Carmel, Indiana.

The accompanying unaudited condensed consolidated financial statements include our wholly-owned subsidiaries' accounts and have been prepared in accordance with generally accepted accounting principles in the United States of America for interim periods and pursuant to the rules and regulations of the U.S. Securities and Exchange Commission ("SEC"). Certain information and footnote disclosures, including significant accounting policies, normally included in a complete presentation of financial statements prepared in accordance with those principles, rules and regulations have been omitted. The Condensed Consolidated Balance Sheet as of December 31, 2009 was derived from audited financial statements but, as presented in this report, may not include all disclosures required by accounting principles generally accepted in the United States. Arrangements where we may have a variable interest in another party are evaluated in accordance with the provisions of Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC" or "Codification") 810, "Consolidation" ("ASC 810"), to determine whether we would be required to include the financial results of the other party in our consolidated financial statements. As of March 31, 2010, we were not required to include the financial results of any variable interest entity in our condensed consolidated financial statements.

In the fourth quarter of 2009, we changed our accounting for direct costs that relate to the enrollment of new students ("Direct Marketing Costs") to expense those costs in the period incurred. As required under the guidance for voluntary changes in accounting principles, our comparative condensed consolidated financial statements presented for the three months ended March 31, 2009 have been adjusted to apply our new accounting principle for Direct Marketing Costs retrospectively. See our Annual Report on Form 10-K for the fiscal year ended December 31, 2009 filed with the SEC for a more detailed discussion of our change in accounting principle for Direct Marketing Costs.

In the opinion of our management, the financial statements contain all adjustments necessary to fairly state our financial condition and results of operations. The interim financial information should be read in conjunction with the audited consolidated financial statements and notes thereto contained in our Annual Report on Form 10-K as filed with the SEC for the year ended December 31, 2009.

2. New Accounting Guidance

In March 2010, the FASB issued Accounting Standards Update ("ASU") No. 2010-11, which is included in the Codification under ASC 815, "Derivatives and Hedging" ("ASC 815"). This update clarifies the type of embedded credit derivative that is exempt from embedded derivative bifurcation requirements. Only an embedded credit derivative that is related to the subordination of one financial instrument to another qualifies for the exemption. This guidance became effective for our interim and annual reporting periods beginning January 1, 2010. The adoption of this guidance did not have a material impact on our condensed consolidated financial statements.

In February 2010, the FASB issued ASU No. 2010-09, which is included in the Codification under ASC 855, “Subsequent Events” (“ASC 855”). This update removes the requirement for an SEC filer to disclose the date through which subsequent events have been evaluated and became effective for our interim and annual reporting periods beginning January 1, 2010. The adoption of this guidance did not have a material impact on our condensed consolidated financial statements.

In January 2010, the FASB issued ASU No. 2010-06, which is included in the Codification under ASC 820, “Fair Value Measurements and Disclosures” (“ASC 820”). This update requires the disclosure of transfers between the observable input categories and activity in the unobservable input category for fair value measurements. The guidance also requires disclosures about the inputs and valuation techniques used to measure fair value and became effective for our interim and annual reporting periods beginning January 1, 2010. The adoption of this guidance did not have a material impact on our condensed consolidated financial statements.

In June 2009, the FASB set forth certain requirements to improve the financial reporting by enterprises involved with variable interest entities and to provide more relevant and reliable information to users of financial statements. This guidance was included in the Codification under ASC 810 and became effective for our interim and annual reporting periods beginning January 1, 2010. The adoption of this guidance did not have a material impact on our condensed consolidated financial statements.

Also in June 2009, the FASB provided guidance to improve transparency about transfers of financial assets and a transferor’s continuing involvement, if any, with transferred financial assets. It also clarified the requirement for isolation and limitations on portions of financial assets that are eligible for sale accounting, eliminated exceptions for qualifying special-purpose entities from the consolidation guidance and eliminated the exception that permitted sale accounting for certain mortgage securitizations when a transferor has not surrendered control over the financial assets. This guidance was included in the Codification under ASC 860, “Transfers and Servicing” (“ASC 860”), and became effective for our interim and annual reporting periods beginning January 1, 2010. The adoption of this guidance did not have a material impact on our condensed consolidated financial statements.

### 3. Fair Value

Fair value for financial reporting is defined as the price that would be received upon the sale of an asset or paid upon the transfer of a liability in an orderly transaction between market participants at the measurement date. The fair value measurement of our financial assets utilized assumptions categorized as observable inputs under the accounting guidance. Observable inputs are assumptions based on independent market data sources.

The following table sets forth information regarding the fair value measurement of our financial assets as of March 31, 2010:

| Description            | As of<br>March<br>31, 2010 | Fair Value Measurements at Reporting Date  |  |  |
|------------------------|----------------------------|--|--|--|
|                        |                            | (Level 1)<br>Quoted<br>Prices in<br>Active<br>Markets for<br>Identical<br>Assets | Using<br>(Level 2)<br>Significant<br>Other<br>Observable<br>Inputs | (Level 3)<br>Significant<br>Unobservable<br>Inputs |
| Cash equivalents       | \$ 165,187                 | \$ 165,187   | \$ --  | \$ --  |
| Short-term investments | 156,143                    | 80,686   | 75,457   | --   |

|            |            |           |       |
|------------|------------|-----------|-------|
| \$ 321,330 | \$ 245,873 | \$ 75,457 | \$ -- |
|------------|------------|-----------|-------|

We used quoted prices in active markets for identical assets as of the measurement date to value our financial assets that were categorized as Level 1. For assets that were categorized as Level 2, we used:

- quoted prices for similar assets in active markets;
- quoted prices for identical or similar assets in markets that were not active or in which little public information had been released;
- inputs other than quoted prices that were observable for the assets; or
- inputs that were principally derived from or corroborated by observable market data by correlation or other means.

The carrying amounts for cash and cash equivalents, restricted cash, accounts receivable, accounts payable, other accrued liabilities and deferred revenue approximate fair value because of the immediate or short-term maturity of these financial instruments. Investments classified as available-for-sale are recorded at their market value.

The fair value of the notes receivable and escrow accounts included in Other assets on our Condensed Consolidated Balance Sheet as of March 31, 2010 is estimated by discounting the future cash flows using current rates for similar arrangements or the market price for the instrument. As of March 31, 2010, each of the carrying value and the estimated fair value of these financial instruments was approximately \$19,400.

The fair value of our long-term debt is estimated by discounting the future cash flows using current rates for similar loans with similar characteristics and remaining maturities. As of March 31, 2010, each of the carrying value and the estimated fair value of our long-term debt was approximately \$150,000.

#### 4. Equity Compensation

The stock-based compensation expense and related income tax benefit recognized in our Condensed Consolidated Statements of Income in the periods indicated were as follows:

|                                  | Three Months Ended |             |
|----------------------------------|--------------------|-------------|
|                                  | March 31,          |             |
|                                  | 2010               | 2009        |
| Stock-based compensation expense | \$ 4,813           | \$ 4,183    |
| Income tax (benefit)             | \$ (1,853 )        | \$ (1,611 ) |

We did not capitalize any stock-based compensation cost in the three months ended March 31, 2010 or 2009.

As of March 31, 2010, we estimated that pre-tax compensation expense for unvested stock-based compensation grants in the amount of approximately \$26,514, net of estimated forfeitures, will be recognized in future periods. This expense will be recognized over the remaining service period applicable to the grantees which, on a weighted-average basis, is approximately 2.3 years.

The stock options granted, forfeited, exercised and expired in the period indicated were as follows:

| # of      | Three Months Ended March 31, 2010 |                          |   |                               |
|-----------|-----------------------------------|--------------------------|---|-------------------------------|
|           | Weighted Average Exercise Price   | Aggregate Exercise Price | Weighted Average Remaining Contractual Term | Aggregate Intrinsic Value (1) |
| Shares    | Price                             | Price                    | Term  | Value (1)                     |
| 1,605,806 | \$ 67.31                          | \$ 108,094               |   |                               |

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|                                    |           |           |            |           |           |
|------------------------------------|-----------|-----------|------------|-----------|-----------|
| Outstanding at beginning of period |           |           |            |           |           |
| Granted                            | 305,000   | \$ 113.41 | 34,590     |           |           |
| Forfeited                          | --        | \$ --     | --         |           |           |
| Exercised                          | (32,129 ) | \$ 31.93  | (1,026 )   |           |           |
| Expired                            | (4,601 )  | \$ 49.99  | (230 )     |           |           |
| Outstanding at end of period       | 1,874,076 | \$ 75.47  | \$ 141,428 | 4.9 years | \$ 69,368 |
| Exercisable at end of period       | 1,308,790 | \$ 59.95  | \$ 78,466  | 3.8 years | \$ 68,746 |

(1) The aggregate intrinsic value of the stock options was calculated by multiplying the number of shares subject to the options outstanding or exercisable, as applicable, by the closing market price of our common stock on March 31, 2010, and subtracting the applicable aggregate exercise price.

The following table sets forth information regarding the stock options granted and exercised in the periods indicated:

|  | Three Months Ended<br>March 31, |           |
|--|---------------------------------|-----------|
|  | 2010                            | 2009      |
| Shares subject to stock options granted            | 305,000                         | 258,000   |
| Weighted average grant date fair value             | \$ 43.59                        | \$ 54.05  |
| Shares subject to stock options exercised          | 32,129                          | 139,444   |
| Intrinsic value of stock options exercised         | \$ 2,430                        | \$ 10,710 |
| Proceeds received from stock options exercised     | \$ 1,026                        | \$ 5,823  |
| Tax benefits realized from stock options exercised | \$ 923                          | \$ 3,970  |

The intrinsic value of a stock option is the difference between the fair market value of the stock and the option exercise price.

The fair value of each stock option grant was estimated on the date of grant using the following assumptions:

|                           | Three Months<br>Ended March 31, |      |
|---------------------------|---------------------------------|------|
|                           | 2010                            | 2009 |
| Risk-free interest rates  | 2.2%                            | 1.6% |
| Expected lives (in years) | 4.6                             | 4.5  |
| Volatility                | 43%                             | 54%  |
| Dividend yield            | None                            | None |

The following table sets forth the number of restricted stock units ("RSUs") that were granted, forfeited and vested in the period indicated:

Three Months Ended  
March 31, 2010  
# of RSUs

|                                 |           | Weighted<br>Average<br>Grant Date<br>Fair Value |
|---------------------------------|-----------|---|
| Unvested at beginning of period | 125,550   | \$ 92.31  |
| Granted                         | 37,639    | \$ 110.81                                       |
| Forfeited                       | (1,714 )  | \$ 105.23                                       |
| Vested                          | (18,740 ) | \$ 77.60  |
| Unvested at end of period       | 142,735   | \$ 98.97  |

The total fair market value of the RSUs vested during the three months ended March 31, 2010 was \$1,817.

#### 5. Stock Repurchases

As of March 31, 2010, 4,541,725 shares remained available for repurchase under the share repurchase program (the “Repurchase Program”) authorized by our Board of Directors. The terms of the Repurchase Program provide that we may repurchase shares of our common stock, from time to time depending on market conditions and other considerations, in the open market or through privately negotiated transactions in accordance with Rule 10b-18 of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Unless earlier terminated by our Board of Directors, the Repurchase Program will expire when we repurchase all shares authorized for repurchase thereunder.

The following table sets forth information regarding the shares of our common stock that we repurchased in the periods indicated:

|                        | Three Months Ended<br>March 31, |           |
|------------------------|---------------------------------|-----------|
|                        | 2010                            | 2009      |
| Number of shares       | 952,500                         | 527,833   |
| Total cost             | \$ 95,025                       | \$ 64,360 |
| Average cost per share | \$ 99.76                        | \$ 121.93 |

#### 6. Debt

We are a party to a Second Amended and Restated Credit Agreement dated as of January 11, 2010 and amended as of February 3, 2010 (the “Credit Agreement”) with two unaffiliated lenders to borrow up to \$150,000 under two revolving credit facilities: one in the maximum principal amount of \$50,000; and the other in the maximum principal amount of \$100,000. We can borrow under the credit facilities on either a secured or unsecured basis at our election, except if an event that would be a default under the Credit Agreement has occurred and is continuing, we may not elect to borrow on an unsecured basis. Both revolving credit facilities under the Credit Agreement mature on May 1, 2012.

Borrowings under the Credit Agreement bear interest, at our option, at the London Interbank Offered Rate (“LIBOR”) plus an applicable margin or at an alternative base rate, as defined under the Credit Agreement. We pay a facility fee equal to 0.30% per annum on the daily amount of the commitment of each lender (whether used or unused). As of March 31, 2010, the borrowings under the Credit Agreement were \$150,000, all of which were secured and bore interest at a rate of 0.725% per annum. Approximately \$157,950 of our investments and cash equivalents served as collateral for the secured borrowings as of March 31, 2010.

The following table sets forth the interest expense (including the facility fee) that we recognized on our borrowings under the Credit Agreement and under the prior credit agreement that was replaced by the Credit Agreement in the periods indicated:



|                  | Three Months<br>Ended<br>March 31,<br>2010 |        | 2009 |
|------------------|--|--------|------|
| Interest expense | \$ 420                                     | \$ 189 |      |

## 7. Investments

The following table sets forth how our investments were classified on our Condensed Consolidated Balance Sheets as of the dates indicated:

|                        | As of:             |             |            | As of:             |             |            | As of:             |             |            |
|------------------------|--------------------|-------------|------------|--------------------|-------------|------------|--------------------|-------------|------------|
|                        | March 31, 2010     |             |            | December 31, 2009  |             |            | March 31, 2009     |             |            |
|                        | Available-for-Sale | At-Maturity | Total      | Available-for-Sale | At-Maturity | Total      | Available-for-Sale | At-Maturity | Total      |
| Short-term investments | \$ 150,965         | \$ --       | \$ 150,965 | \$ 138,270         | \$ --       | \$ 138,270 | \$ 141,048         | \$ --       | \$ 141,048 |

The following table sets forth the aggregate fair value, amortized cost basis and the net unrealized gains and losses included in accumulated other comprehensive income (loss) of our available-for-sale investments as of the dates indicated:

|                                 | As of:               |                |                               | As of:               |                |                               | As of:               |                |                      |
|---------------------------------|----------------------|----------------|-------------------------------|----------------------|----------------|-------------------------------|----------------------|----------------|----------------------|
|                                 | March 31, 2010       |                |                               | December 31, 2009    |                |                               | March 31, 2009       |                |                      |
|                                 | Aggregate Fair Value | Amortized Cost | Net Unrealized Gains (Losses) | Aggregate Fair Value | Amortized Cost | Net Unrealized Gains (Losses) | Aggregate Fair Value | Amortized Cost | Net Unrealized Gains |
| Available-for-Sale Investments: |                      |                |                               |                      |                |                               |                      |                |                      |
| Variable rate demand notes      | \$ 15,000            | \$ 15,000      | \$--                          | \$--                 | \$--           | \$--                          | \$--                 | \$--           | \$--                 |
| Government obligations          | 80,686               | 80,712         | (26)                          | 81,591               | 81,634         | (43)                          | 66,134               | 66,061         | 73                   |
| Government agency obligations   | 31,430               | 31,454         | (24)                          | 27,932               | 27,969         | (37)                          | 37,144               | 37,085         | 59                   |
| Corporate obligations           | 23,849               | 23,814         | 35                            | 28,747               | 28,690         | 57                            | 37,770               | 37,731         | 39                   |
|                                 | \$ 150,965           | \$ 150,980     | \$(15)                        | \$ 138,270           | \$ 138,293     | \$(23)                        | \$ 141,048           | \$ 140,877     | \$ 171               |

We also held a certificate of deposit with a total principal value of \$5,178 as of March 31, 2010, \$5,137 as of December 31, 2009 and \$5,014 as of March 31, 2009. This investment is included in short-term investments on our Condensed Consolidated Balance Sheet.

The following table sets forth the unrealized gains and losses on available-for-sale investments that were included in other comprehensive income (loss) in the periods indicated:

|                   | Three Months Ended March<br>31, |           |
|-------------------|---------------------------------|-----------|
|                   | 2010                            | 2009      |
| Unrealized gains  | \$ 8                            | \$ --     |
| Unrealized losses | \$ --                           | \$ (257 ) |

No unrealized gains or losses were reclassified out of our accumulated other comprehensive income (loss) during the three months ended March 31, 2010 and 2009. We recognized \$93 of investment gains in our Condensed Consolidated Statement of Income for the three months ended March 31, 2010.

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The following table sets forth the components of investment income included in interest income in our Condensed Consolidated Statements of Income in the periods indicated:

|   | Three Months Ended |          |
|---|--------------------|----------|
|   | March 31,          |          |
|   | 2010               | 2009     |
| Interest income on investments            | \$ 153             | \$ 1,233 |
| Realized gains on the sale of investments | 93                 | --       |
|   | \$ 246             | \$ 1,233 |

The following table sets forth the contractual maturities of our debt securities classified as available-for-sale as of March 31, 2010:

| Contractual Maturity                   | Available-for-Sale |
|--|--------------------|
| Due within five years                  | \$ 135,965         |
| Due after five years through ten years | --                 |
| Due after ten years                    | 15,000             |
|  | \$ 150,965         |

8. Notes Receivable

On January 20, 2010, we entered into an arrangement to purchase a subordinated note from an unaffiliated trust in connection with the PEAKS Private Student Loan Program (the "PEAKS Program"), a new private education loan program for our students. Under the PEAKS Program, an unaffiliated lender makes private education loans to eligible students and, subsequently, sells those loans to a trust.

We transfer to the trust a portion of the amount of each private student loan disbursed to us under the PEAKS Program, in exchange for a subordinated note issued by the trust to us. The trust also issued senior debt in the aggregate principal amount of \$300,000 (the "Senior Debt") to investors. The trust utilizes the proceeds from the issuance of the subordinated note and the Senior Debt to purchase private education loans made by the unaffiliated lender to our students. The subordinated note does not bear interest, and principal is due on the subordinated note following the repayment of the Senior Debt and the payment of fees, expenses and certain reimbursement obligations of the trust. The carrying value of the subordinated note as of March 31, 2010 was not material.

As a result of this arrangement and our guarantee to the trust as described in Note 11, we held a variable interest in the trust, but we are not considered the primary beneficiary for purposes of including the financial results of the trust in our consolidated financial statements.

Beginning in the second quarter of 2009, we made advances to another unaffiliated third party, the purpose of which is to purchase private education loans and sell participation interests in those loans. The third party used the advances from us to provide partial funding for private education loans made to our students. The carrying value of the note due to us from this third party as of March 31, 2010 was approximately \$12,710. The note bears interest at a rate based on the prime rate plus an applicable margin. Substantially all of the assets of the third party serve as collateral for the note. The note is subject to customary terms and conditions and may be repaid at any time without penalty prior to its 2025 maturity date.

As a result of these advances, we held a variable interest in this third party, but we are not considered the primary beneficiary for purposes of including the financial results of this third party in our consolidated financial statements.

9. Earnings Per Common Share

Earnings per common share for all periods have been calculated in conformity with ASC 260, "Earnings Per Share". This data is based on historical net income and the weighted average number of shares of our common stock outstanding during each period as set forth in the following table:

|  | Three Months Ended |        |
|--|--------------------|--------|
|  | March 31,          |        |
|  | 2010               | 2009   |
|  | (In thousands)     |        |
| <b>Shares:</b>   |                    |        |
| Weighted average number of shares of common stock outstanding      | 35,028             | 38,558 |
| Shares assumed issued (less shares assumed purchased for treasury) |                    |        |
| for stock-based compensation                                       | 471                | 504    |
| Outstanding shares for diluted earnings per share calculation      | 35,499             | 39,062 |

A total of 577,000 shares at March 31, 2010 and 272,374 shares at March 31, 2009 were excluded from the calculation of our diluted earnings per common share because the effect was anti-dilutive.

#### 10. Employee Pension Benefits

The following table sets forth the components of net periodic pension cost (benefit) of the ESI Pension Plan and ESI Excess Pension Plan for the periods indicated:

|                                     | Three Months    |        |
|-------------------------------------|-----------------|--------|
|                                     | Ended March 31, |        |
|                                     | 2010            | 2009   |
| Interest cost                       | \$ 720          | \$ 774 |
| Expected return on assets           | (1,110 )        | (954 ) |
| Recognized net actuarial loss       | 377             | 566    |
| Amortization of prior service cost  | 7               | 7      |
| Net periodic pension cost (benefit) | \$ (6 )         | \$ 393 |

The benefit accruals under the ESI Pension Plan and ESI Excess Pension Plan were frozen effective March 31, 2006. As a result, no service cost has been included in the net periodic pension cost or benefit.

We made no contributions to the ESI Pension Plan or the ESI Excess Pension Plan during the three months ended March 31, 2010 and 2009. We do not expect to make any contributions to the ESI Pension Plan or the ESI Excess Pension Plan in 2010.

#### 11. Contingencies

As part of our normal operations, one of our insurers issues surety bonds for us that are required by various education authorities that regulate us. We are obligated to reimburse our insurer for any of those surety bonds that are paid by the insurer. As of March 31, 2010, the total face amount of those surety bonds was approximately \$21,375.

We are also subject to various claims and contingencies in the ordinary course of our business, including those related to litigation, business transactions, employee-related matters and taxes, among others. We cannot assure you of the ultimate outcome of any litigation involving us. Any litigation alleging violations of education or consumer protection laws and/or regulations, misrepresentation, fraud or deceptive practices may also subject our affected campuses to

additional regulatory scrutiny.

Guarantees. We entered into a guarantee agreement and related documents in connection with the PEAKS Program. Under the PEAKS Program, an unaffiliated lender makes private education loans to eligible students and, subsequently, sells those loans to a trust. The trust has issued Senior Debt in the aggregate principal amount of \$300,000 to investors. The assets of the trust (which include, among other assets, the student loans held by the trust) will serve as collateral for, and are intended to be the principal source of, the repayment of the Senior Debt. The Senior Debt bears interest at a variable rate based on the LIBOR plus an applicable margin and matures in January 2020.

Under the guarantee agreement, we guarantee payment of principal, interest and certain call premiums on the Senior Debt, and administrative fees and expenses of the trust. The guarantee agreement contains, among other things, representations and warranties and events of default customary for guarantees. In addition, under the PEAKS Program, some or all of the holders of the Senior Debt could require us to purchase their Senior Debt in certain limited circumstances that pertain to our continued eligibility to participate in the federal student financial aid programs under Title IV of the Higher Education Act of 1965, as amended (the "Title IV Programs"). We believe that the likelihood of those limited circumstances occurring is remote. Our guarantee and purchase obligations under the PEAKS Program remain in effect until the Senior Debt and the trust's fees and expenses are paid in full. At such time, we will be entitled to repayment of the amount of any payments made under our guarantee to the extent that funds are remaining in the trust.

The maximum future payments that we could be required to make under the guarantee agreement include:

- up to \$300,000 in principal of Senior Debt;
- accrued interest on the Senior Debt;
- certain call premiums associated with the Senior Debt; and
- the fees and expenses of the trust.

We are not able to estimate the undiscounted maximum potential amount of future payments that we could be required to make under the guarantee agreement, because those payments will be affected by:

- the amount of the private education loans made under the PEAKS Program;
- the fact that those loans will consist of a large number of loans of individually immaterial amounts;
- the repayment performance of those loans, the proceeds from which will be used to repay the Senior Debt and to pay the fees and expenses of the trust;
- the fact that the interest rate on the Senior Debt is a variable rate based on the LIBOR plus a margin;
- whether certain call premiums will be payable in connection with the Senior Debt; and
- the amount of fees and expenses of the trust.

In February 2009, we entered into an agreement with an unaffiliated third party whereby private education loans are provided to our students to help pay the students' cost of education that student financial aid from federal, state and other sources do not cover (the "Private Student Loan Program"). In connection with the Private Student Loan Program, we entered into a risk sharing agreement (the "2009 RSA") under which we have guaranteed the repayment of any private education loans that are charged off above a certain percentage of the private education loans made under the Private Student Loan Program, based on the annual dollar volume. As of March 31, 2010, the outstanding balance of the private education loans made under the Private Student Loan Program was approximately \$75,000. Our obligations under the 2009 RSA will remain in effect until all private education loans made under the Private Student Loan Program are paid in full or charged off. The standard repayment term for a private education loan made under the Private Student Loan Program is ten years, with repayment generally beginning six months after a student graduates or three months after a student withdraws or is terminated from his or her program of study.

Pursuant to the 2009 RSA, we are required to maintain collateral to secure our guarantee obligation in an amount equal to a percentage of the outstanding balance of the private education loans disbursed to our students under the Private Student Loan Program. As of March 31, 2010, the total collateral maintained in a restricted bank account was not material. This amount is included in Other assets on our Condensed Consolidated Balance Sheet as of March 31, 2010. The 2009 RSA also requires that we comply with certain covenants, including that we maintain certain financial ratios which are measured on a quarterly basis. We were in compliance with these covenants as of March 31, 2010.

We also are a party to a separate risk sharing agreement (the "2007 RSA") with a different lender for certain private education loans that were made to our students in 2007 and early 2008. We guaranteed the repayment of any private education loans that the lender charges off above a certain percentage of the total dollar volume of private education loans made under this agreement. We will have the right to pursue repayment from the borrowers for those charged off private education loans under the 2007 RSA that we pay to the lender pursuant to our guarantee obligation. The 2007 RSA was terminated effective February 22, 2008, such that no private education loans have been or will be made under the 2007 RSA after that date. Our obligations under the 2007 RSA will remain in effect until all private education loans under the agreement are paid in full or charged off by the lender.

The maximum future payments that we could be required to make pursuant to our guarantee obligation under the 2007 RSA are affected by:

- the amount of the private education loans made under the 2007 RSA;
- the fact that those loans consist of a large number of loans of individually immaterial amounts;
  - the interest and fees associated with those loans;
  - the repayment performance of those loans; and
  - when during the life of the loans they are charged off.

As a result, we are not able to estimate the undiscounted maximum potential future payments that we could be required to make under the 2007 RSA.

As of March 31, 2010, we had not made any guarantee payments under the PEAKS Program, the 2009 RSA or the 2007 RSA, and our recorded liability for the guarantee obligations related to those arrangements was not material.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

#### Forward-Looking Statements

All statements, trend analyses and other information contained in this report that are not historical facts are forward-looking statements within the meaning of the safe harbor provision of the Private Securities Litigation Reform Act of 1995 and as defined in Section 27A of the Securities Act of 1933 (the "Securities Act") and Section 21E of the Exchange Act. Forward-looking statements are made based on our management's current expectations and beliefs concerning future developments and their potential effects on us. You can identify those statements by the use of words such as "could," "should," "would," "may," "will," "project," "believe," "anticipate," "expect," "plan," "estimate," "potential," "intend," "continue" and "contemplate," as well as similar words and expressions. Forward-looking statements involve risks and uncertainties and do not guarantee future performance. We cannot assure you that future developments affecting us will be those anticipated by our management. Among the factors that could cause actual results to differ materially from those expressed in our forward-looking statements are the following:

- business conditions and growth in the postsecondary education industry and in the general economy;
- changes in federal and state governmental regulations with respect to education and accreditation standards, or the interpretation or enforcement of those regulations, including, but not limited to, the level of government funding for, and our eligibility to participate in, student financial aid programs utilized by our students;

- our failure to comply with the extensive education laws and regulations and accreditation standards that we are subject to;
- effects of any change in our ownership resulting in a change in control, including, but not limited to, the consequences of such changes on the accreditation and federal and state regulation of our campuses;
  - our ability to implement our growth strategies;
  - our failure to maintain or renew required regulatory authorizations or accreditation of our campuses;
    - receptivity of students and employers to our existing program offerings and new curricula;
      - loss of access by our students to lenders for student loans;
      - our ability to collect internally funded financing from our students;
    - our exposure under our guarantees related to private student loan programs; and
    - our ability to successfully defend litigation and other claims brought against us.

Readers are also directed to other risks and uncertainties discussed in other documents we file with the SEC, including, without limitation, those discussed in Item 1A. "Risk Factors." of our Annual Report on Form 10-K for the fiscal year ended December 31, 2009 filed with the SEC. We undertake no obligation to update or revise any forward-looking information, whether as a result of new information, future developments or otherwise.

#### Overview

You should keep in mind the following points as you read this report:

- References in this document to "we," "us," "our" and "ITT/ESI" refer to ITT Educational Services, Inc. and its subsidiaries.
- The terms "ITT Technical Institute" or "Daniel Webster College" (in singular or plural form) refer to an individual campus owned and operated by ITT/ESI, including its learning sites, if any. The terms "institution" or "campus group" (in singular or plural form) mean a main campus and its additional locations, branch campuses and/or learning sites, if any.

This management's discussion and analysis of financial condition and results of operations should be read in conjunction with the same titled section contained in our Annual Report on Form 10-K for the fiscal year ended December 31, 2009 filed with the SEC for discussion of, among other matters, the following items:

- cash receipts from financial aid programs;
- nature of capital additions;
- seasonality of revenue;
- components of income statement captions;
- federal regulations regarding:
  - timing of receipt of funds from the Title IV Programs;
- percentage of applicable revenue that may be derived from the Title IV Programs;
- return of Title IV Program funds for withdrawn students; and
  - default rates;
  - private loan programs;
  - investments; and
- repurchase of shares of our common stock.

This management's discussion and analysis of financial condition and results of operations is based on our condensed consolidated financial statements, which have been prepared in conformity with generally accepted accounting principles in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amount of assets, liabilities, revenue, expenses, and contingent assets and liabilities. Actual results may differ from those estimates and judgments under different assumptions or conditions.

The financial information discussed in this management's discussion and analysis of financial condition and results of operations related to the three months ended March 31, 2009 are as adjusted to reflect the effect of our change in accounting principle for Direct Marketing Costs. See our Annual Report on Form 10-K for the fiscal year ended December 31, 2009 filed with the SEC for a more detailed discussion of our change in accounting principle for Direct Marketing Costs.

In this management's discussion and analysis of financial condition and results of operations, when we discuss factors that contributed to a change in our financial condition or results of operations, we disclose the primary factors that materially contributed to that change.

## Background

We are a leading provider of technology-oriented postsecondary education programs in the United States based on revenue and student enrollment. As of March 31, 2010, we were offering master, bachelor and associate degree programs to more than 84,000 students. As of March 31, 2010, we had 127 locations (including 123 campuses and four learning sites) in 38 states. All of our locations are authorized by the applicable education authorities of the states in which they operate, and are accredited by an accrediting commission recognized by the ED. We design our education programs, after consultation with employers, to help graduates prepare for careers in various fields involving their areas of study. We have provided career-oriented education programs since 1969 under the "ITT Technical Institute" name and since June 2009 under the "Daniel Webster College" name.

In the first quarter of 2010, we began operations at two new ITT Technical Institute campuses. We plan to begin operations at six to eight additional locations during the remainder of 2010. Our overall expansion plans include:

- offering a broader range of both residence and online programs at our existing campuses;
- increasing the number of our campuses that offer bachelor degree programs; and
- adding learning sites to existing campuses.

## Critical Accounting Policies and Estimates

The preparation of our condensed consolidated financial statements requires us to make estimates and judgments that affect the reported amount of assets, liabilities, revenue, expenses, and contingent assets and liabilities. Actual results may differ from those estimates and judgments under different assumptions or conditions. We have discussed the critical accounting policies that we believe affect our more significant estimates and judgments used in the preparation of our consolidated financial statements in the "Management's Discussion and Analysis of Financial Condition and Results of the Operations – Critical Accounting Policies and Estimates" section of our Annual Report on Form 10-K for the fiscal year ended December 31, 2009 filed with the SEC. There have been no material changes to those critical accounting policies or the underlying accounting estimates or judgments.

## New Accounting Guidance

In March 2010, the FASB issued ASU No. 2010-11, which is included in the Codification under ASC 815. This update clarifies the type of embedded credit derivative that is exempt from embedded derivative bifurcation requirements. Only an embedded credit derivative that is related to the subordination of one financial instrument to another qualifies for the exemption. This guidance became effective for our interim and annual reporting periods beginning January 1, 2010. The adoption of this guidance did not have a material impact on our condensed consolidated financial statements.

In February 2010, the FASB issued ASU No. 2010-09, which is included in the Codification under ASC 855. This update removes the requirement for an SEC filer to disclose the date through which subsequent events have been

evaluated and became effective for our interim and annual reporting periods beginning January 1, 2010. The adoption of this guidance did not have a material impact on our condensed consolidated financial statements.

In January 2010, the FASB issued ASU No. 2010-06, which is included in the Codification under ASC 820. This update requires the disclosure of transfers between the observable input categories and activity in the unobservable input category for fair value measurements. The guidance also requires disclosures about the inputs and valuation techniques used to measure fair value and became effective for our interim and annual reporting periods beginning January 1, 2010. The adoption of this guidance did not have a material impact on our condensed consolidated financial statements.

In June 2009, the FASB set forth certain requirements to improve the financial reporting by enterprises involved with variable interest entities and to provide more relevant and reliable information to users of financial statements. This guidance was included in the Codification under ASC 810 and became effective for our interim and annual reporting periods beginning January 1, 2010. The adoption of this guidance did not have a material impact on our condensed consolidated financial statements.

Also in June 2009, the FASB provided guidance to improve transparency about transfers of financial assets and a transferor's continuing involvement, if any, with transferred financial assets. It also clarified the requirement for isolation and limitations on portions of financial assets that are eligible for sale accounting, eliminated exceptions for qualifying special-purpose entities from the consolidation guidance and eliminated the exception that permitted sale accounting for certain mortgage securitizations when a transferor has not surrendered control over the financial assets. This guidance was included in the Codification under ASC 860 and became effective for our interim and annual reporting periods beginning January 1, 2010. The adoption of this guidance did not have a material impact on our condensed consolidated financial statements.

## Results of Operations

The following table sets forth the percentage relationship of certain statement of income data to revenue for the periods indicated:

|  | Three Months Ended |        |
|--|--------------------|--------|
|  | March 31,          |        |
|  | 2010               | 2009   |
| Revenue                                      | 100.0%             | 100.0% |
| Cost of educational services                 | 35.0%              | 35.1%  |
| Student services and administrative expenses | 27.9%              | 30.7%  |
| Operating income                             | 37.1%              | 34.2%  |
| Interest income, net                         | 0.1%               | 0.4%   |
| Income before provision for income taxes     | 37.2%              | 34.6%  |

The following table sets forth our total student enrollment as of the dates indicated:

|              | 2010                     |                          | 2009                        |                             |
|--------------|--------------------------|--------------------------|-----------------------------|-----------------------------|
|              | Total Student Enrollment | Increase Over Prior Year | Total Student Enrollment(1) | Increase Over Prior Year(1) |
| of: March 31 | 84,555                   | 28.9%                    | 65,620                      | 21.1%                       |
| June 30      |                          |                          | 69,889                      | 27.6%                       |



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|              |                |                |        |       |
|--------------|----------------|----------------|--------|-------|
|              | Not applicable | Not applicable |        |       |
| September 30 | Not applicable | Not applicable | 79,208 | 28.7% |
| December 31  | Not applicable | Not applicable | 80,766 | 30.3% |

(1) Students enrolled at Daniel Webster College have been included beginning with the June 30, 2009 period.

Total student enrollment includes all new and continuing students. A continuing student is any student who, in the academic term being measured, is enrolled in a program of study at one of our campuses and was enrolled in the same program at any of our campuses at the end of the immediately preceding academic term. A new student is any student who, in the academic term being measured, enrolls in and begins attending any program of study at one of our campuses:

- for the first time at that campus;
- after graduating in a prior academic term from a different program of study at that campus; or
- after having withdrawn or been terminated from a program of study at that campus.

The following table sets forth our new student enrollment in the periods indicated:

| New Student Enrollment in the Three Months Ended: | 2010                   |                          | 2009                      |                             |
|---|------------------------|--------------------------|---------------------------|-----------------------------|
|   | New Student Enrollment | Increase Over Prior Year | New Student Enrollment(1) | Increase Over Prior Year(1) |
| March 31  | 23,064                 | 21.8%                    | 18,935                    | 36.8%                       |
| June 30   | Not applicable         | Not applicable           | 19,692                    | 33.5%                       |
| September 30                                      | Not applicable         | Not applicable           | 27,738                    | 27.2%                       |
| December 31                                       | Not applicable         | Not applicable           | 19,563                    | 31.2%                       |
| Total for the year                                | Not applicable         | Not applicable           | 85,928                    | 31.6%                       |

(1) New students enrolled at Daniel Webster College have been included beginning with the September 30, 2009 period.

We believe that economic downturns in the United States, in particular those that result in higher unemployment rates among unskilled workers, have historically been associated with increased student enrollment at postsecondary educational institutions. Based on this, we believe that the current economic recession in the United States which has given rise to higher unemployment among unskilled workers has contributed to the year-over-year increases in our new and total student enrollment in each of the past several fiscal quarters. These increases have had a material favorable effect on our results of operations, cash flows and financial condition. There are a number of other factors, however, that affect student enrollment, and we cannot assure you that this trend will continue or we will continue to experience similar financial and operating results. In addition, tighter credit markets in the United States have contributed to reduced availability of private education loans from third-party lenders to our students and, as a result, have led to an increase in the amount of internal student financing that we have provided to our students and an increase in the level of guarantees that we have provided to third parties related to private education loans made to our

students.

At the vast majority of our campuses, we generally organize the academic schedule for programs of study offered on the basis of four 12-week academic quarters in a calendar year. The academic quarters typically begin in early March, mid-June, early September and late November or early December. To measure the persistence of our students, the number of continuing students in any academic term is divided by the total student enrollment in the immediately preceding academic term.

The following table sets forth the rates of our students' persistence as of the dates indicated:

| Year | Student Persistence as of (1): |                |                |                |
|------|--------------------------------|----------------|----------------|----------------|
|      | March 31                       | June 30        | September 30   | December 31    |
| 2008 | 76.1%                          | 73.9%          | 72.5%          | 76.5%          |
| 2009 | 75.3%                          | 75.3%          | 73.6%          | 77.3%          |
| 2010 | 76.1%                          | Not applicable | Not applicable | Not applicable |

(1) Students enrolled at Daniel Webster College have been included beginning with the rate as of September 30, 2009. The impact of our students' persistence as a result of the inclusion of Daniel Webster College students in the calculation was not material.

Three Months Ended March 31, 2010 Compared with Three Months Ended March 31, 2009. Revenue increased \$95.9 million, or 33.3%, to \$384.0 million in the three months ended March 31, 2010 compared to \$288.0 million in the three months ended March 31, 2009. The primary factors that contributed to this increase included, in order of significance:

- a 30.3% increase in total student enrollment at December 31, 2009 compared to December 31, 2008;
  - a 5.0% increase in tuition rates implemented in March 2010 and March 2009; and
- a 28.9% increase in total student enrollment at March 31, 2010 compared to March 31, 2009.

The primary factors that contributed to the increase in student enrollment included, in order of significance:

- student enrollment growth in programs of study and at locations that were in operation prior to 2008;
  - new programs of study offered at our campuses; and
  - operating new campuses.

Cost of educational services increased \$33.3 million, or 32.9%, to \$134.4 million in the three months ended March 31, 2010 compared to \$101.1 million in the three months ended March 31, 2009. The primary factors that contributed to this increase included, in order of significance:

- the costs required to service the increased total student enrollment; and
- increased costs associated with operating new campuses.

The increase in cost of educational services was partially offset by greater leverage of our fixed costs in the operation of our campuses.

Cost of educational services as a percentage of revenue decreased 10 basis points to 35.0% in the three months ended March 31, 2010 compared to 35.1% in the three months ended March 31, 2009. The primary factor that contributed to this decrease was greater leverage of our fixed costs in the operation of our campuses. The decrease in cost of educational services as a percentage of revenue was partially offset by the costs associated with operating new

campuses.

Student services and administrative expenses increased \$18.5 million, or 20.9%, to \$107.0 million in the three months ended March 31, 2010 compared to \$88.5 million in the three months ended March 31, 2009. The principal causes of this increase included, in order of significance:

- an increase in bad debt expense associated with increases in the amount of internal student financing; and
  - an increase in compensation and benefit costs associated with a greater number of employees.

Student services and administrative expenses decreased to 27.9% of revenue in the three months ended March 31, 2010 compared to 30.7% of revenue in the three months ended March 31, 2009. The principal cause of this decrease was our ability to leverage our centralized services over a larger base of operations and media advertising costs increasing at a lower rate than the increase in revenue. The decrease in student services and administrative expenses as a percentage of revenue was partially offset by an increase in bad debt expense. Bad debt expense as a percentage of revenue increased to 5.9% in the three months ended March 31, 2010, compared to 4.9% in the three months ended March 31, 2009. The primary factor that contributed to this increase was an increase in the amount of internal student financing that we provided to our students due to increased student enrollment. We believe that our bad debt expense as a percentage of revenue will be in the range of 4.0% to 6.0% in 2010, primarily as a result of the amount of internal student financing that we provide to our students not increasing at the same rate as the increase in student enrollment due to the private loan programs available to our students in 2010.

Operating income increased \$44.1 million, or 44.8%, to \$142.6 million in the three months ended March 31, 2010 compared to \$98.5 million in the three months ended March 31, 2009, as a result of the impact of the factors discussed above in connection with revenue, cost of educational services, and student services and administrative expenses. Our operating margin increased to 37.1% in the three months ended March 31, 2010 compared to 34.2% in the three months ended March 31, 2009, as a result of the impact of the factors discussed above.

Interest income decreased \$0.5 million, or 42.5%, to \$0.7 million in the three months ended March 31, 2010 compared to \$1.2 million in the three months ended March 31, 2009, primarily due to a change in the investment mix and lower average investment balances. Interest expense increased \$0.2 million, or 116.5%, to \$0.4 million in the three months ended March 31, 2010 compared to \$0.2 million in the three months ended March 31, 2009, due to an increase in the effective interest rate on our revolving credit facilities.

Our combined federal and state effective income tax rate was 38.8% in the three month periods ended March 31, 2010 and March 31, 2009.

#### Financial Condition, Liquidity and Capital Resources

Cash and cash equivalents were \$165.5 million as of March 31, 2010 compared to \$128.8 million as of December 31, 2009 and \$219.6 million as of March 31, 2009. We also had short-term investments of \$156.1 million as of March 31, 2010 compared to \$143.4 million as of December 31, 2009 and \$146.1 million as of March 31, 2009. In total, our cash and cash equivalents and short-term investments were \$321.7 million as of March 31, 2010 compared to \$272.2 million as of December 31, 2009 and \$365.7 million as of March 31, 2009. The \$49.5 million increase in cash and cash equivalents and short-term investments as of March 31, 2010 compared to December 31, 2009 was primarily due to cash generated from operations which was partially offset by repurchases of our common stock. The \$44.0 million decrease in cash and cash equivalents and short-term investments as of March 31, 2010 compared to March 31, 2009 was primarily due to repurchases of our common stock which was partially offset by cash generated from operations.

We are required to recognize the funded status of our defined benefit postretirement plans on our balance sheet. We recorded an asset of \$3.8 million for the ESI Pension Plan, a non-contributory defined benefit pension plan commonly referred to as a cash balance plan, and a liability of \$0.3 million for the ESI Excess Pension Plan, a nonqualified,

unfunded retirement plan, on our Condensed Consolidated Balance Sheet as of March 31, 2010.

We do not expect to make any contributions to the ESI Pension Plan or the ESI Excess Pension Plan in 2010. In 2009, we contributed \$0.5 million to the ESI Excess Pension Plan and made no contributions to the ESI Pension Plan.

Operations. Cash from operating activities was \$159.1 million in the three months ended March 31, 2010 compared to \$61.3 million in the three months ended March 31, 2009. The \$97.8 million increase in operating cash flow was primarily due to higher student enrollments.

Accounts receivable less allowance for doubtful accounts was \$88.3 million as of March 31, 2010 compared to \$51.5 million as of March 31, 2009. Days sales outstanding was 20.7 days at March 31, 2010 and 16.1 days at March 31, 2009. Both increases were primarily due to increases in internal student financing resulting from increased student enrollment. We believe that our days sales outstanding at the end of 2010 will be in the range of 10 to 15 days, primarily as a result of the amount of internal student financing that we provide to our students not increasing at the same rate as the increase in student enrollment due to the private loan programs available to our students in 2010.

Investing. In the three months ended March 31, 2010, we spent \$0.8 million to renovate and expand buildings at nine of our locations, compared to \$1.1 million for similar expenditures at eight of our locations in the three months ended March 31, 2009.

Capital expenditures, excluding facility and land purchases and facility construction, totaled \$5.3 million in the three months ended March 31, 2010 compared to \$4.6 million in the three months ended March 31, 2009. These expenditures consisted primarily of classroom and laboratory equipment (such as computers and electronic equipment), classroom and office furniture, software and leasehold improvements. We plan to continue to upgrade and expand our current facilities and equipment in 2010. Cash generated from operations is expected to be sufficient to fund our capital expenditure requirements.

Financing. We are a party to the Credit Agreement which provides that we may borrow up to \$150.0 million under two revolving credit facilities: one in the maximum principal amount of \$50.0 million; and the other in the maximum principal amount of \$100.0 million. Borrowings under the Credit Agreement are used to allow us to continue repurchasing shares of our common stock while maintaining compliance with certain financial ratios required by the ED, the state education authorities that regulate our locations and the accrediting agencies that accredit our locations.

Both revolving credit facilities under the Credit Agreement mature on May 1, 2012. The borrowings under each credit facility may be secured or unsecured at our election, except if an event that would be a default under the Credit Agreement has occurred and is continuing, we may not elect to borrow on an unsecured basis. Cash equivalents and investments held in a pledged account serve as the collateral for any secured borrowings under the Credit Agreement.

The availability of borrowings under the Credit Agreement is subject to our ability at the time of borrowing to satisfy certain specified conditions. These conditions include the absence of default by us, as defined in the Credit Agreement, and that the representations and warranties contained in the Credit Agreement and related loan documents continue to be true and correct. Under the Credit Agreement, we are also required to maintain:

- a certain maximum leverage ratio at the end of each of our fiscal quarters;
- a monthly minimum ratio of cash and investments to indebtedness; and
- a minimum ED financial responsibility composite ratio as of the end of each fiscal year.

We were in compliance with the applicable ratio requirements as of March 31, 2010.

Borrowings under the Credit Agreement bear interest, at our option, at LIBOR plus an applicable margin or at an alternative base rate as defined under the Credit Agreement. We pay a facility fee equal to 0.30% per annum on the

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daily amount of the commitment of each lender (whether used or unused). As of March 31, 2010, the borrowings under the Credit Agreement were \$150.0 million, all of which were secured, and bore interest at a rate of 0.725% per annum. Approximately \$158.0 million of our investments and cash equivalents served as collateral for the secured borrowings as of March 31, 2010.

Our Board of Directors has authorized us to repurchase shares of our common stock in the open market or through privately negotiated transactions in accordance with Rule 10b-18 of the Exchange Act under the Repurchase Program. The following table sets forth information regarding our share repurchase activity in the periods indicated:

|                         | Three Months Ended March 31,                  |           |
|-------------------------|---|-----------|
|                         | 2010  | 2009      |
|                         | (Dollars in thousands, except per share data) |           |
| Number of shares        | 952,500                                       | 527,833   |
| Total cost              | \$ 95,025                                     | \$ 64,360 |
| Average price per share | \$ 99.76                                      | \$ 121.93 |

Approximately 4.5 million shares remained available for repurchase under the Repurchase Program as of March 31, 2010. Pursuant to the Board's stock repurchase authorization, we plan to repurchase additional shares of our common stock from time to time in the future depending on market conditions and other considerations.

We believe that cash generated from operations and our investments will be adequate to satisfy our working capital, loan repayment and capital expenditure requirements for the foreseeable future. We also believe that any reduction in cash and cash equivalents or investments that may result from their use to provide student financing, purchase facilities, construct facilities, repay loans or repurchase shares of our common stock will not have a material adverse effect on our expansion plans, planned capital expenditures, ability to meet any applicable regulatory financial responsibility standards or ability to conduct normal operations.

#### Contractual Obligations

The following table sets forth our specified contractual obligations as of March 31, 2010:

| Contractual Obligations                               | Total      | Payments Due by Period |              |              |                      |
|---|------------|------------------------|--------------|--------------|----------------------|
|   |            | Less than<br>1 Year    | 1-3<br>Years | 3-5<br>Years | More than<br>5 Years |
| (In thousands)  |            |                        |              |              |                      |
| Operating lease obligations                           | \$ 182,861 | \$ 42,737              | \$ 74,672    | \$ 49,208    | \$ 16,244            |
| Long-term debt, including scheduled interest payments | \$ 153,246 | \$ 1,559               | \$ 151,687   | \$ --        | \$ --                |
| Total   | \$ 336,107 | \$ 44,296              | \$ 226,359   | \$ 49,208    | \$ 16,244            |

The long-term debt represents our revolving credit facilities under the Credit Agreement and assumes that the \$150.0 million outstanding balance under the facilities as of March 31, 2010 will be outstanding at all times through the date of maturity. The amounts shown include the principal payments that will be due upon maturity as well as interest payments and facility fees. Interest payments have been calculated based on their scheduled payment dates using the interest rate charged on our borrowings as of March 31, 2010.

#### Off-Balance Sheet Arrangements

As of March 31, 2010, we leased our non-owned facilities under operating lease agreements. A majority of the operating leases contain renewal options that can be exercised after the initial lease term. Renewal options are

generally for periods of one to five years. All operating leases will expire over the next 14 years and management believes that:

- those leases will be renewed or replaced by other leases in the normal course of business;
  - we may purchase the facilities represented by those leases; or
  - we may purchase or build other replacement facilities.

There are no material restrictions imposed by the lease agreements, and we have not entered into any significant guarantees related to the leases. We are required to make additional payments under the terms of certain operating leases for taxes, insurance and other operating expenses incurred during the operating lease period.

As part of our normal course of operations, one of our insurers issues surety bonds for us that are required by various education authorities that regulate us. We are obligated to reimburse our insurer for any of those surety bonds that are paid by the insurer. As of March 31, 2010, the total face amount of those surety bonds was approximately \$21.4 million.

On January 20, 2010, we entered into a guarantee agreement and related documents in connection with the PEAKS Program. Under the PEAKS Program, an unaffiliated lender makes private education loans to our eligible students and, subsequently, sells those loans to a trust. The trust has issued Senior Debt in the aggregate principal amount of \$300.0 million to investors. The assets of the trust (which include, among other assets, the student loans held by the trust) will serve as collateral for, and are intended to be the principal source of, the repayment of the Senior Debt. The Senior Debt bears interest at a variable rate based on the LIBOR plus a margin and matures in January 2020.

In connection with the PEAKS Program, we transfer to the trust a portion of the amount of each private student loan disbursed to us, in exchange for a subordinated note issued by the trust to us. The subordinated note does not bear interest, and principal is due on the subordinated note following the repayment of the Senior Debt, the payment of fees and expenses of the trust and the reimbursement of the amount of any payments made by us under the guarantee agreement. The carrying value of the subordinated note on our Condensed Consolidated Balance Sheet as of March 31, 2010 was not material. The trust utilizes the proceeds from the issuance of the Senior Debt and the subordinated note to purchase the student loans from the lender.

Under the guarantee agreement, we guarantee payment of principal, interest and certain call premiums on the Senior Debt, and administrative fees and expenses of the trust. The guarantee agreement contains, among other things, representations and warranties and events of default customary for guarantees. In addition, under the PEAKS Program, some or all of the holders of the Senior Debt could require us to purchase their Senior Debt in certain limited circumstances that pertain to our continued eligibility to participate in the Title IV Programs. We believe that the likelihood of those limited circumstances occurring is remote. Our guarantee and purchase obligations under the PEAKS Program remain in effect until the Senior Debt and the trust's fees and expenses are paid in full. At such time, we will be entitled to repayment of the amount of any payments made under our guarantee and payment of the subordinated note, in each case only to the extent of available funds remaining in the trust.

In February 2009, we entered into the Private Student Loan Program. In connection with the Private Student Loan Program, we entered into the 2009 RSA under which we have guaranteed the repayment of any private education loans that are charged off above a certain percentage of the private education loans made under the Private Student Loan Program, based on the annual dollar volume. As of March 31, 2010, the outstanding balance of the private education loans made under the Private Student Loan Program was approximately \$75.0 million. Our obligations under the 2009 RSA will remain in effect until all private education loans made under the Private Student Loan Program are paid in full or charged off. The standard repayment term for a private education loan made under the Private Student Loan Program is ten years, with repayment generally beginning six months after a student graduates or three months after a student withdraws or is terminated from his or her program of study.

Pursuant to the 2009 RSA, we are required to maintain collateral to secure our guarantee obligation in an amount equal to a percentage of the outstanding balance of the private education loans disbursed to our students under the Private Student Loan Program. As of March 31, 2010, the total collateral maintained in a restricted bank account was not material. The 2009 RSA also requires that we comply with certain covenants, including that we maintain certain financial ratios which are measured on a quarterly basis. We were in compliance with these covenants as of March 31, 2010.

In addition, beginning in the second quarter of 2009, we made advances to the unaffiliated third party that is holding the private education loans made to our students under the Private Student Loan Program. We made the advances, which bear interest, so that the third party could use those funds to provide additional funding for the private education loans, instead of retaining the funds ourselves and providing internal student financing, which is non-interest bearing. The carrying value of the note due to us from this third party on our Condensed Consolidated Balance Sheet as of March 31, 2010 was approximately \$12.7 million. The note bears interest at a rate based on the prime rate plus an applicable margin. Substantially all of the assets of the third party serve as collateral for the note. The note is subject to customary terms and conditions and may be repaid at any time without penalty prior to its 2025 maturity date.

We also are a party to the 2007 RSA with a different lender for certain private education loans that were made to our students in 2007 and early 2008. We guaranteed the repayment of any private education loans that the lender charges off above a certain percentage of the total dollar volume of private education loans made under this agreement. We will have the right to pursue repayment from the borrowers for those charged off private education loans under the 2007 RSA that we pay to the lender pursuant to our guarantee obligation. The 2007 RSA was terminated effective February 22, 2008, such that no private education loans have been or will be made under the 2007 RSA after that date. Our obligations under the 2007 RSA will remain in effect until all private education loans under the agreement are paid in full or charged off by the lender.

As of March 31, 2010, we had not made any guarantee payments under the PEAKS Program, the 2009 RSA or the 2007 RSA, and our recorded liability for the guarantee obligations related to those arrangements was not material.

Based on the prior repayment history of our students with respect to private education loans and current economic conditions, we do not believe that our guarantee obligations under either RSA or the PEAKS Program will have a material adverse effect on our financial condition, results of operations or cash flows. See Note 11 of the Notes to Condensed Consolidated Financial Statements for further discussion of the PEAKS Program, the 2009 RSA and the 2007 RSA.

### Item 3. Quantitative and Qualitative Disclosures about Market Risk.

In the normal course of our business, we are subject to fluctuations in interest rates that could impact the return on our investments and the cost of our financing activities. Our primary interest rate risk exposure results from changes in short-term interest rates and the LIBOR.

Our investments consist primarily of government and governmental obligations and marketable debt securities. We estimate that the market risk associated with these investments can best be measured by a potential decrease in the fair value of these investments from a hypothetical 10% increase in interest rates. If such a hypothetical increase in rates were to occur, the reduction in the market value of our portfolio of marketable securities would not be material.

Changes in the LIBOR would affect the borrowing costs associated with our revolving credit facilities. We estimate that the market risk can best be measured by a hypothetical 100 basis point increase in the LIBOR. If such a hypothetical increase in the LIBOR were to occur, the effect on our results from operations and cash flow would not have been material for the three months ended March 31, 2010.

Item 4. Controls and Procedures.

(a) Evaluation of Disclosure Controls and Procedures.

We are responsible for establishing and maintaining disclosure controls and procedures (“DCP”) that are designed to ensure that information required to be disclosed by us in the reports filed by us under the Exchange Act is: (a) recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms; and (b) accumulated and communicated to our management, including our principal executive and principal financial officers, to allow timely decisions regarding required disclosures. In designing and evaluating our DCP, we recognize that any controls and procedures, no matter how well designed and implemented, can provide only reasonable assurance of achieving the desired control objectives, and that our management’s duties require it to make its best judgment regarding the design of our DCP. As of the end of our first fiscal quarter of 2010, we conducted an evaluation, under the supervision (and with the participation) of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our DCP pursuant to Rule 13a-15 of the Exchange Act. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our DCP were effective.

(b) Changes in Internal Control Over Financial Reporting.

There were no changes in our internal control over financial reporting that occurred during our most recently completed fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II  
OTHER INFORMATION

Item 1. Legal Proceedings.

We are subject to various claims and contingencies in the ordinary course of our business, including those related to litigation, business transactions, employee-related matters and taxes, among others. We cannot assure you of the ultimate outcome of any litigation involving us. Any litigation alleging violations of education or consumer protection laws and/or regulations, misrepresentation, fraud or deceptive practices may also subject our affected campuses to additional regulatory scrutiny.

Item 1A. Risk Factors.

You should carefully consider the risks and uncertainties we describe in our Annual Report on Form 10-K for the fiscal year ended December 31, 2009 before deciding to invest in, or retain, shares of our common stock. These are not the only risks and uncertainties that we face. Additional risks and uncertainties that we do not currently know about, we currently believe are immaterial or we have not predicted may also harm our business operations or adversely affect us. If any of these risks or uncertainties actually occurs, our business, financial condition, results of operations or cash flows could be materially adversely affected. There have been no material changes from the risk factors discussed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2009.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

The following table sets forth information regarding purchases made by us of shares of our common stock on a monthly basis in the three months ended March 31, 2010:



## Issuer Purchases of Equity Securities

| Period   | Total<br>Number of<br>Shares<br>Purchased | Average<br>Price Paid<br>per Share | Total<br>Number of<br>Shares<br>Purchased<br>as Part of<br>Publicly<br>Announced<br>Plans<br>or<br>Programs<br>(1) | Maximum<br>Number of<br>Shares that May<br>Yet Be<br>Purchased<br>Under the Plans<br>or<br>Programs (1) |
|--|---|------------------------------------|--|---|
| January 1, 2010<br>through January 31,<br>2010   | 6,926 (2)                                 | \$ 96.89                           | --   | 5,494,225   |
| February 1, 2010<br>through February 28,<br>2010 | 952,504 (3)                               | 99.76                              | 952,500  | 4,541,725   |
| March 1, 2010 through<br>March 31, 2010          | 36 (2)                                    | 112.58                             | --   | 4,541,725   |
| Total  | 959,466 (4)                               | \$ 99.74                           | 952,500  |   |

(1) Our Board of Directors has authorized us to repurchase the following number of shares of our common stock pursuant to the Repurchase Program:

| Number of<br>Shares | Board<br>Authorization<br>Date |
|---------------------|--------------------------------|
| 2,000,000           | April 1999                     |
| 2,000,000           | April 2000                     |
| 5,000,000           | October 2002                   |
| 5,000,000           | April 2006                     |
| 5,000,000           | April 2007                     |
| 5,000,000           | January 2010                   |

The shares that remained available for repurchase under the Repurchase Program were 4,541,725 as of March 31, 2010. The terms of the Repurchase Program provide that we may repurchase shares of our common stock, from time to time depending on market conditions and other considerations, in the open market or through privately negotiated transactions in accordance with Rule 10b-18 of the Exchange Act. Unless earlier terminated by our Board of Directors, the Repurchase Program will expire when we repurchase all shares authorized for repurchase thereunder.

- (2) These shares of our common stock were tendered to us by employees to satisfy the income tax obligations associated with the vesting of certain equity awards granted to those employees.
- (3) Includes four shares of our common stock that were tendered to us by employees to satisfy the income tax obligations associated with the vesting of certain equity awards granted to those employees.
- (4) Includes 6,966 shares of our common stock that were tendered to us by employees to satisfy the income tax obligations associated with the vesting of certain equity awards granted to those employees.

Item 6. Exhibits.

A list of exhibits required to be filed as part of this report is set forth in the Index to Exhibits, which immediately precedes the exhibits, and is incorporated herein by reference.

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SIGNATURES

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

ITT  
Educational  
Services, Inc.

Date: April  
22, 2010

By: /s/ Daniel  
M.  
Fitzpatrick  
Daniel M.  
Fitzpatrick  
Executive  
Vice  
President,  
Chief  
Financial  
Officer  
(Duly  
Authorized  
Officer,  
Principal  
Financial  
Officer  
and Principal  
Accounting  
Officer)

## INDEX TO EXHIBITS

| Exhibit<br>No. | Description   |
|----------------|---|
| 3.1            | Restated Certificate of Incorporation, as Amended to Date (incorporated herein by reference from the same exhibit number to ITT/ESI's 2005 second fiscal quarter report on Form 10-Q)   |
| 3.2            | Restated By-Laws, as Amended to Date (incorporated herein by reference from the same exhibit number to ITT/ESI's current report on Form 8-K dated January 19, 2009)   |
| 10.1           | Second Amended and Restated Credit Agreement, dated as of January 11, 2010, among ITT Educational Services, Inc., JPMorgan Chase Bank, N.A. and Bank of America, N.A. (incorporated herein by reference from Exhibit 10.64 to ITT/ESI's Current Report on Form 8-K filed on January 12, 2010) |
| 10.2           | First Amendment to Second Amended and Restated Credit Agreement, dated as of February 3, 2010, among ITT Educational Services, Inc., JPMorgan Chase Bank, N.A. and Bank of America, N.A. (incorporated herein by reference from Exhibit 10.36 to ITT/ESI's 2009 Annual Report on Form 10-K)   |
| 31.1           | Chief Executive Officer's Certification Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934   |
| 31.2           | Chief Financial Officer's Certification Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934   |
| 32.1           | Chief Executive Officer's Certification Pursuant to 18 U.S.C. Section 1350  |
| 32.2           | Chief Financial Officer's Certification Pursuant to 18 U.S.C. Section 1350  |