ITT Educational Services, Inc.

Consolidated Financial Statements
At December 31, 2010 and 2009 and for each of
the Three Years in the Period Ended December 31, 2010

ITT Educational Services, Inc.
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December 31, 2010 and 2009

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Appendix I

Management's Report on Internal Control over Financial Reporting

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of
ITT Educational Services, Inc.:

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of ITT Educational Services, Inc. and its subsidiaries (the "Company") at December 31, 2010 and 2009, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2010 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2010, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management's Report on Internal Control Over Financial Reporting appearing in Appendix I. Our responsibility is to express opinions on these financial statements, , and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

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

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

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Indianapolis, Indiana
February 17, 2011

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

	As of December 31,	
	2010	**2009**
Assets		
Current assets:		
Cash and cash equivalents	$163,779	$128,788
Short-term investments	149,160	143,407
Restricted cash	255	1,891
Accounts receivable, less allowance for doubtful accounts of $7,526 and $25,227	68,937	85,426
Deferred income taxes	9,079	13,799
Prepaid expenses and other current assets	22,887	17,651
Total current assets	414,097	390,962
Property and equipment, net	198,213	195,449
Deferred income taxes	21,814	6,416
Other assets	40,656	23,878
Total assets	$674,780	$616,705
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable	$67,920	$61,275
Accrued compensation and benefits	28,428	26,323
Other current liabilities	15,441	25,261
Deferred revenue	244,362	171,933
Total current liabilities	356,151	284,792
Long-term debt	150,000	150,000
Other liabilities	40,559	25,328
Total liabilities	546,710	460,120
Commitments and contingent liabilities (Note 12)		
Shareholders' equity:		
Preferred stock, $.01 par value, 5,000,000 shares authorized, none issued	0	0
Common stock, $.01 par value, 300,000,000 shares authorized, 37,068,904 and 54,068,904 issued	371	541
Capital surplus	173,935	154,495
Retained earnings	524,678	1,006,903
Accumulated other comprehensive (loss)	(4,509)	(10,093)
Treasury stock, 7,075,563 and 18,622,809 shares, at cost	(566,405)	(995,261)
Total shareholders' equity	128,070	156,585
Total liabilities and shareholders' equity	$674,780	$616,705

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

ITT EDUCATIONAL SERVICES, INC.
CONSOLIDATED STATEMENTS OF INCOME
(Amounts in thousands, except per share data)

	Year Ended December 31,		
	2010	**2009**	**2008**
Revenue	$1,596,529	$1,319,194	$1,015,333
Costs and expenses:			
Cost of educational services	537,855	449,835	383,769
Student services and administrative expenses	445,125	380,567	306,099
Total costs and expenses	982,980	830,402	689,868
Operating income	613,549	488,792	325,465
Interest income	2,504	3,291	6,505
Interest (expense)	(1,918)	(726)	(4,611)
Income before provision for income taxes	614,135	491,357	327,359
Provision for income taxes	239,969	191,094	125,854
Net income	$374,166	$300,263	$201,505
Earnings per share:			
Basic	$11.28	$8.01	$5.18
Diluted	$11.17	$7.91	$5.13
Weighted average shares outstanding:			
Basic	33,165	37,490	38,881
Diluted	33,501	37,942	39,243

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

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

	Year Ended December 31,		
	2010	**2009**	**2008**
Cash flows from operating activities:			
Net income	$374,166	$300,263	$201,505
Adjustments to reconcile net income to net cash flows from operating activities:			
Depreciation and amortization	26,797	24,908	22,230
Provision for doubtful accounts	86,935	81,983	43,286
Deferred income taxes	(14,557)	(3,066)	(9,389)
Excess tax benefit from stock option exercises	(3,383)	(5,289)	(1,158)
Stock-based compensation expense	15,813	13,074	7,235
Other	468	(1,163)	1,554
Changes in operating assets and liabilities, net of acquisition:			
Restricted cash	1,636	5,775	(4,350)
Accounts receivable	(70,446)	(136,837)	(57,933)
Accounts payable	6,645	4,911	9,695
Other operating assets and liabilities	62,057	6,344	11,205
Deferred revenue	72,429	10,355	(50,921)
Net cash flows from operating activities	558,560	301,258	172,959
Cash flows from investing activities:			
Facility expenditures and land purchases	(6,118)	(4,236)	(18,093)
Capital expenditures, net	(26,811)	(23,992)	(17,543)
Acquisition of college, net of cash acquired	0	(20,792)	0
Proceeds from sales and maturities of investments and repayment of notes	385,306	247,701	1,085,559
Purchase of investments and note advances	(451,594)	(263,012)	(920,480)
Net cash flows from investing activities	(99,217)	(64,331)	129,443
Cash flows from financing activities:			
Excess tax benefit from stock option exercises	3,383	5,289	1,158
Proceeds from exercise of stock options	7,893	8,800	3,241
Repurchase of common stock and shares tendered for taxes	(435,628)	(348,483)	(87,774)
Net cash flows from financing activities	(424,352)	(334,394)	(83,375)
Net change in cash and cash equivalents	34,991	(97,467)	219,027
Cash and cash equivalents at beginning of period	128,788	226,255	7,228
Cash and cash equivalents at end of period	$163,779	$128,788	$226,255
Supplemental disclosures of cash flow information:			
Cash paid during the period for:			
Income taxes (net of refunds)	$259,788	$190,718	$123,223
Interest	$1,914	$824	$5,036
Non-cash financing activities:			
Issuance of treasury stock for Directors compensation	$ 30	$30	$60

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

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

	Common Stock		Capital	Retained	Accumulated Other Comprehensive	Common Stock in Treasury		
	Shares	Amount	Surplus	Earnings	Income (Loss)	Shares	Amount	Total
Balance as of December 31, 2007	54,069	$541	$127,017	$518,823	($3,417)	(14,375)	($584,946)	$58,018
Net income				201,505				201,505
Other comprehensive income:								
Prior service costs, net of $10 of income tax					17			17
Net actuarial pension loss, net of $7,237 of income tax					(11,212)			(11,212)
Pension settlement loss, net of $599 of income tax					928			928
Unrealized gain					428			428
Comprehensive income								191,666
Prior service costs, net of $83 of income tax					(128)			(128)
Adoption of change in pension measurement date, net of $210 of income tax				325				325
Exercise of stock options and equity awards				(2,528)		75	5,769	3,241
Tax benefit from exercise of stock options			1,201					1,201
Stock-based compensation			7,235					7,235
Common shares repurchased						(1,050)	(87,774)	(87,774)
Issuance of shares for Directors' compensation				(25)		1	85	60
Restricted stock cancellations			202			(3)	(202)	0
Balance as of December 31, 2008	54,069	541	135,655	718,100	(13,384)	(15,352)	(667,068)	173,844
Net income				300,263				300,263
Other comprehensive income:								
Prior service costs, net of $11 of income tax					17			17
Net actuarial pension loss, net of $2,386 of income tax					3,697			3,697
Pension settlement loss, net of $18 of income tax					28			28
Unrealized (loss)					(451)			(451)
Comprehensive income								303,554
Exercise of stock options and equity awards				(11,462)		210	20,262	8,800
Tax benefit from exercise of stock options and equity award vesting			5,766					5,766
Stock-based compensation			13,074					13,074
Common shares repurchased						(3,478)	(348,123)	(348,123)
Issuance of shares for Directors' compensation				2		1	28	30
Shares tendered for taxes						(4)	(360)	(360)
Balance as of December 31, 2009	54,069	541	154,495	1,006,903	(10,093)	(18,623)	(995,261)	156,585
Net income				374,166				374,166
Other comprehensive income:								
Prior service costs, net of $4,058 of income tax					6,340			6,340
Net actuarial pension loss, net of $551 of income tax					(860)			(860)
Unrealized gain					104			104
Comprehensive income								379,750
Exercise of stock options and equity awards				(13,631)		214	21,524	7,893
Tax benefit from exercise of stock options and equity award vesting			3,627					3,627
Stock-based compensation			15,813					15,813
Common shares repurchased						(5,658)	(434,656)	(434,656)
Issuance of shares for Directors' compensation				1		1	29	30
Shares tendered for taxes						(10)	(972)	(972)
Common shares retired	(17,000)	(170)		(842,761)		17,000	842,931	0
Balance as of December 31, 2010	37,069	$371	$173,935	$524,678	($4,509)	(7,076)	($566,405)	$128,070

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

1. Business and Significant Accounting Policies

Business. We are a leading proprietary provider of postsecondary education in the United States based on revenue and student enrollment. As of December 31, 2010, we were offering master, bachelor and associate degree programs to approximately 84,000 students and had 134 locations (including 130 campuses and four learning sites) in 38 states. In addition, we offered one or more of our online programs to students who are located in 48 states and the District of Columbia. We have provided career-oriented education programs since 1969 under the "ITT Technical Institute" name and since June 2009 under the "Daniel Webster College" ("DWC") name. Our corporate headquarters are located in Carmel, Indiana.

Basis of Presentation. The 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 ("GAAP") and pursuant to the rules and regulations of the U.S. Securities and Exchange Commission ("SEC"). All significant intercompany balances and transactions are eliminated upon consolidation. 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 December 31, 2010, we were not required to include the financial results of any variable interest entity in our consolidated financial statements. Certain reclassifications have been made in the consolidated financial statements of prior years to conform to the current year presentation. These reclassifications have no impact on previously reported net income, total shareholders' equity or cash flows.

Use of Estimates. The preparation of these consolidated financial statements, in accordance with GAAP, includes estimates and assumptions that are determined by our management. Actual results could differ materially from the estimates. Significant accounting estimates and assumptions are used for, but not limited to:

- the allowance for doubtful accounts;
- useful lives of tangible and intangible assets;
- self insurance;
- pension liabilities;
- stock-based compensation;
- unrecognized tax benefits; and
- litigation exposures.

Cash Equivalents. Highly liquid investments purchased with an original maturity of three months or less are considered cash equivalents.

Restricted Cash. The funds from the federal student financial aid programs under Title IV ("Title IV Programs") of the Higher Education Act of 1965, as amended ("HEA"), and certain other monies transferred to us by electronic funds transfer are subject to holding restrictions, generally from three to seven days, before they can be drawn into our cash account. The funds subject to these holding periods are identified as restricted cash until they are applied to the students' accounts. In addition, the state education regulations in one state require us to maintain an escrow account as a condition to operating our campus in that state. We also maintain an escrow account for a guarantee obligation to an unaffiliated third party under a private education loan program for our students. The funds in both of these escrow accounts are considered restricted cash and classified as other assets. The aggregate balance in these escrow accounts as of December 31, 2010 and December 31, 2009 was not material.

Investments. We classify our investments in marketable securities as available-for-sale or held-to-maturity depending on our investment intentions with regard to those securities on the date of acquisition. Investments are classified as either current or non-current based on the maturity date of each security.

The cost of securities sold is based on the specific identification method.

Accounts Receivable and Allowance for Doubtful Accounts. We extend unsecured credit to our students for tuition and fees and we record a receivable for the tuition and fees earned in excess of the payment received from or on behalf of a student. The individual student balances of these receivables are insignificant. We record an allowance for doubtful accounts with respect to accounts receivable based on the students' credit profiles and our historical collection experience related to amounts owed by our students with similar credit profiles. If our collection trends were to differ significantly from our historical collection experience, we would make a corresponding adjustment to our allowance for doubtful accounts.

When a student is no longer enrolled in a program of study at one of our campuses, we increase the allowance for doubtful accounts related to the former student's receivable balance to reflect the amount we estimate will not be collected. The amount that we estimate will not be collected is based on a review of the historical collection experience for each campus, adjusted as needed to reflect other facts and circumstances. We review the collection activity after a student withdraws or graduates from a campus and will write off the accounts receivable if we conclude that collection of the balance is not probable.

Property and Equipment. Property and equipment is recorded in our consolidated financial statements at cost, less accumulated depreciation and amortization. Maintenance and repairs are expensed as incurred. Expenditures that extend the useful lives of our assets are capitalized.

Developed or purchased software is capitalized in accordance with ASC 350, "Intangibles – Goodwill and Other." Facility construction costs are capitalized as incurred, with depreciation commencing when the facility is placed in service. We capitalize interest on our real estate construction projects in accordance with ASC 835, "Interest."

Provisions for depreciation and amortization of property and equipment have generally been made using the straight-line method over the following ranges of useful lives:

Type of Property and Equipment	Estimated Useful Life
Furniture and equipment	3 to 10 years
Leasehold, building and land improvements	3 to 14 years
Buildings	20 to 40 years
Software	3 to 8 years

We amortize leasehold improvements using the straight-line method over the shorter of the life of the improvement or the term of the underlying lease. Land is not depreciated.

We regularly review our long-lived assets for impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. If we determine that the carrying amount of a long-lived asset exceeds the total amount of the estimated undiscounted future cash flows from that asset, we would determine the fair value of that asset using a discounted cash flows model. If the amount of discounted cash flows is less than the net book value of the long-lived asset, we recognize an impairment loss in the amount of the difference. We base our impairment analyses of long-lived assets on our current business strategy, expected growth rates and estimates of future economic and regulatory conditions.

Insurance Liabilities. We record liabilities and related expenses for medical, workers compensation and other insurance in accordance with the contractual terms of the insurance policies. We record the total liabilities that are estimable and probable as of the reporting date for our insurance liabilities that we self-insure. The accounting for our self-insured arrangements involves estimates and judgments to determine the liability to be recorded for reported claims and claims incurred but not reported. We consider our historical experience in determining the appropriate insurance reserves to record. If our current insurance claim trends were to differ significantly from our historic claim experience, however, we would make a corresponding adjustment to our insurance reserves.

Contingent Liabilities. 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. When we are aware of a claim or potential claim, we assess the likelihood of any loss or exposure. If it is probable that a loss will result and the amount of the loss can be reasonably estimated, we record a liability for the loss. The liability recorded includes probable and estimable legal costs associated with the claim or potential claim. If the loss is not probable or the amount of the loss cannot be reasonably estimated, we disclose the claim if the likelihood of a potential loss is reasonably possible and the amount involved is material.

Guarantees. In accordance with ASC 460, "Guarantees," we recognize a liability for the fair value of a guarantee obligation upon its issuance. We evaluate the fair value of our guarantee obligations periodically and adjust the liability as warranted. The fair market value of our guarantees related to certain private student loan programs were estimated based on historical charge off experience with respect to private loans made to our students and the present value of the expected cash flows, taking into consideration current economic conditions, that may result from the settlement of the guarantee obligations in the future.

Treasury Stock. Repurchases of outstanding shares of our common stock are recorded at cost. Treasury stock issued in fulfillment of stock-based compensation awards or other obligations is accounted for under the last in, first out method. We record "losses" from the sale of treasury stock that exceed previous net "gains" from the sale of treasury stock as a charge to retained earnings.

The retirement of shares of our common stock held in treasury are accounted for under the first in, first out method. We reduce common stock in the amount of the par value of the shares retired and we reduce retained

earnings in the amount of the difference between the cost of the treasury shares and their par value. In November 2010, we retired 17 million shares of our common stock held in treasury that had an aggregate cost of $842,931 and reduced retained earnings by $842,761.

Fair Value and Credit Risk of Financial Instruments. ASC 820, "Fair Value Measurements and Disclosures" ("ASC 820"), defines fair value for financial reporting 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 ASC 820. 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 December 31, 2010:

		Fair Value Measurements at Reporting Date Using		
Description	**As of December 31, 2010**	**(Level 1) Quoted Prices in Active Markets for Identical Assets**	**(Level 2) Significant Other Observable Inputs**	**(Level 3) Significant Unobservable Inputs**
Cash equivalents:				
Money market funds	$163,165	$163,165	$0	$0
Short-term investments:				
U.S. Treasury securities	110,560	110,560	0	0
Government agency obligations	24,394	0	24,394	0
Corporate bonds	8,903	0	8,903	0
Other assets:				
Money market fund	4,372	4,372	0	0
	$311,394	$278,097	$33,297	$0

The following table sets forth information regarding the fair value measurement of our financial assets as of December 31, 2009:

		Fair Value Measurements at Reporting Date Using		
Description	**As of December 31, 2009**	**(Level 1) Quoted Prices in Active Markets for Identical Assets**	**(Level 2) Significant Other Observable Inputs**	**(Level 3) Significant Unobservable Inputs**
Cash equivalents:				
Money market funds	$124,347	$124,347	$0	$0
Short-term investments:				
U.S. Treasury securities	81,591	81,591	0	0
Government agency obligations	27,932	0	27,932	0
Corporate bonds	28,747	0	28,747	0
Other assets:				
Money market fund	3,298	3,298	0	0
	$265,915	$209,236	$56,679	$0

We used quoted prices in active markets for identical assets as of the measurement dates to value our financial assets that were categorized as Level 1. For assets that were categorized in 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 current 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 included in Other assets on our Consolidated Balance Sheet as of December 31, 2010 is estimated by discounting the future cash flows using current rates for similar arrangements. As of December 31, 2010, the carrying value and the estimated fair value of these financial instruments was approximately $18,000.

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 December 31, 2010, the carrying value and the estimated fair value of our long-term debt was approximately $150,000.

Financial instruments that potentially subject us to credit risk consist primarily of accounts receivable, interest-bearing investments and notes receivable. There is no concentration of credit risk of our accounts receivable, as the total is comprised of a large number of individual balances owed by students whose credit profiles vary and who are located throughout the United States. Our interest-bearing investments generally consist of high-quality securities issued by various entities and major financial institutions. Substantially all of the assets of the party to whom we issued one of the notes receivable serve as collateral for the repayment of the note.

Recognition of Revenue. Tuition revenue is recorded on a straight-line basis over the length of the applicable course. If a student withdraws from an institution, the standards of most state education authorities that regulate our institutions, the accrediting commissions that accredit our institutions and our own internal policy limit a student's obligation for tuition and fees to the institution depending on when a student withdraws during an academic term ("Refund Policies"). The terms of the Refund Policies vary by state, and the limitations imposed by the Refund Policies are generally based on the portion of the academic term that has elapsed at the time the student withdraws. Generally, the greater the portion of the academic term that has elapsed at the time the student withdraws, the greater the student's obligation is to the institution for the tuition and fees related to that academic term. We record revenue net of any refunds that result from any applicable Refund Policy. On an individual student basis, tuition earned in excess of cash received is recorded as accounts receivable, and cash received in excess of tuition earned is recorded as deferred revenue.

We do not charge a separate fee for textbooks that students use in their programs of study. We record the cost of these textbooks in prepaid expenses and other current assets and amortize the cost of textbooks on a straight-line basis over the applicable course length. Tool kit sales, and the related cost, are recognized when the student receives the tool kit. Academic fees (which are charged only one time to students on their first day of class attendance) are recognized as revenue on a straight-line basis over the average program length. If a student withdraws from an institution, all unrecognized revenue relating to his or her fees, net of any refunds that result from any applicable Refund Policy, is recognized upon the student's departure. An administrative fee is charged to a student and recognized as revenue when the student withdraws or graduates from a program of study at an institution.

We report 12 weeks of tuition revenue in each of our four fiscal quarters. We standardized the number of weeks of revenue reported in each fiscal quarter, because the timing of student breaks in a calendar quarter can fluctuate from quarter to quarter each year. The total number of weeks of school during each year is 48.

Advertising Costs. We expense all advertising costs as incurred.

Equity-Based Compensation. Stock-based compensation cost for our equity instruments exchanged for employee and director services is measured at the date of grant, based on the calculated fair value of the grant and is recognized as an expense on a straight-line basis over the period of time that the grantee must provide services to us before the stock-based compensation is fully vested. The vesting period is generally the period set forth in the agreement granting the stock-based compensation. Under the terms of our stock-based compensation plans, some grants immediately vest in full when the grantee's employment or service terminates, and, for grants made prior to November 24, 2010, when he or she retires. As a result, in certain circumstances, the period of time that the grantee must provide services to us in order for that stock-based compensation to fully vest may be less than the vesting period set forth in the agreement granting the stock-based compensation. In these instances, compensation expense will be recognized over this shorter period.

We use a binomial option pricing model to determine the fair value of stock options granted and we use the market price of our common stock to determine the fair value of restricted stock and restricted stock units ("RSUs") granted. The binomial option pricing model takes into account the variables defined below:

- "Volatility" is a statistical measure of the extent to which the stock price is expected to fluctuate during a period and combines our historical stock price volatility and the implied volatility as measured by actively traded stock options.
- "Expected life" is the weighted average period that those stock options are expected to remain outstanding, based on the historical patterns of our stock option exercises, as adjusted to reflect the current position-level demographics of the stock option grantees.
- "Risk-free interest rate" is based on interest rates for terms that are similar to the expected life of the stock options.
- "Dividend yield" is based on our historical and expected future dividend payment practices.

We generally issue shares of our common stock from treasury shares upon the exercise of stock options or vesting of RSUs. As of December 31, 2010, 7,075,563 shares of our common stock were held in treasury. Our Board of Directors has authorized us to repurchase outstanding shares of our common stock, but we are unable to determine at this point how many shares we will repurchase over the next 12 months. See Note 4 for additional disclosures regarding our stock repurchases.

Operating Leases. We lease our non-owned facilities under operating lease agreements. Common provisions within our operating lease agreements include:

- renewal options, which can be exercised after the initial lease term;
- rent escalation clauses;
- tenant improvement allowances; and
- rent holidays.

We record the rent expense associated with each operating lease agreement evenly over the term of the lease. The difference between the amount of rent expense recorded and the amount of rent actually paid is recorded as accrued rent, which is included in other liabilities, on our Consolidated Balance Sheets.

Income Taxes. We account for income taxes using the asset and liability method, which requires the recognition of deferred tax assets and liabilities for expected future tax consequences of temporary differences that currently exist between the tax bases and financial reporting bases of our assets and liabilities.

We follow the guidance under ASC 740, "Income Taxes," which prescribes a single, comprehensive model for how a company should recognize, measure, present and disclose in its financial statements uncertain tax positions that the company has taken or expects to take on its tax returns. This guidance requires us to evaluate whether it is more likely than not, based on the technical merits of a tax position, that the benefits resulting from the position will be realized by us.

We record interest and penalties related to unrecognized tax benefits in income tax expense.

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:

	Year Ended December 31,		
	2010	**2009**	**2008**
		(In thousands)	
Shares:			
Weighted average number of shares of common stock outstanding	33,165	37,490	38,881
Shares assumed issued (less shares assumed purchased for treasury) for stock-based compensation	336	452	362
Outstanding shares for diluted earnings per share calculation	33,501	37,942	39,243

A total of 1,002,962 shares for fiscal year 2010, 272,279 shares for fiscal year 2009 and 396,226 shares for fiscal year 2008 have been excluded from the calculation of our diluted earnings per common share because the effect was anti-dilutive.

2. New Accounting Guidance

In December 2010, the FASB issued Accounting Standards Update ("ASU") No. 2010-29, which is included in the Codification under ASC 805, "Business Combinations." This update provides guidance on the disclosure of supplemental pro forma information for business combinations. This guidance became effective for our interim and annual reporting periods beginning January 1, 2011. The adoption of this guidance will not have a material impact on our consolidated financial statements.

Also in December 2010, the FASB issued ASU No. 2010-28, which is included in the Codification under ASC 350, "Intangibles – Goodwill and Other." This update provides guidance on applying the goodwill impairment test for reporting units with zero or negative carrying amounts. This guidance became effective for our interim and annual reporting periods beginning January 1, 2011. The adoption of this guidance will not have a material impact on our consolidated financial statements.

In April 2010, the FASB issued ASU No. 2010-17, which is included in the Codification under ASC 605, "Revenue Recognition." This update provides guidance on the criteria that should be met for determining whether the milestone method of revenue recognition is appropriate. This guidance became effective for our interim and annual reporting periods beginning July 1, 2010. The adoption of this guidance did not have a material impact on our consolidated financial statements.

In March 2010, the FASB issued ASU No. 2010-11, which is included in the Codification under ASC 815, "Derivatives and Hedging." 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 consolidated financial statements.

In February 2010, the FASB issued ASU No. 2010-09, which is included in the Codification under ASC 855, "Subsequent Events." 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 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. This 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 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 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," 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 consolidated financial statements.

3. Equity Compensation Plans

We have adopted the following equity compensation plans, referred to collectively as the "Plans":

- *2006 ITT Educational Services, Inc. Equity Compensation Plan* – Awards may be granted to our employees and directors under the 2006 ITT Educational Services, Inc. Equity Compensation Plan, as amended ("2006 Equity Compensation Plan") in the form of stock options (incentive and nonqualified), stock appreciation rights ("SARs"), restricted stock, RSUs, performance shares, performance units and other stock-based awards as defined in the plan. The maximum number of shares of our common stock that may be issued pursuant to awards under this plan is 4,000,000. Each share underlying stock options and SARs granted and not forfeited or terminated, reduces the number of shares available for future awards by one share. The delivery of a share in connection with a "full-value award" (i.e., an award of restricted stock, RSUs, performance shares, performance units or any other stock-based award with value denominated in shares) reduces the number of shares remaining for other awards by three shares. As of December 31, 2010, restricted stock, RSUs and nonqualified stock options have been awarded under this plan.

- *1999 Outside Directors Stock Option Plan* – A maximum of 500,000 shares of our common stock were available to be issued upon the exercise of nonqualified stock options granted to non-employee directors under the 1999 Outside Directors Stock Option Plan ("1999 Directors Stock Plan").
- *1997 ITT Educational Services, Inc. Incentive Stock Plan* – A maximum of 8,100,000 shares of our common stock were available to be issued upon the exercise of stock options and pursuant to other forms of awards under the 1997 ITT Educational Services, Inc. Incentive Stock Plan ("1997 Stock Plan"), but no more than 20% of the total number of shares on a cumulative basis could have been used for restricted stock or performance share awards. A maximum of 1.5% of our outstanding shares of common stock could have been issued annually, with any unissued shares available to be issued in later years.

No additional awards have been or will be granted after May 9, 2006 under the 1999 Directors Stock Plan or the 1997 Stock Plan.

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

	Year Ended December 31,		
	2010	**2009**	**2008**
Stock-based compensation expense	$15,813	$13,074	$7,235
Income tax (benefit)	($6,089)	($5,034)	($2,785)

We did not capitalize any stock-based compensation cost in the years ended December 31, 2010, 2009 and 2008.

As of December 31, 2010, we estimated that pre-tax compensation expense for unvested stock-based compensation grants in the amount of approximately $15,900, 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 1.8 years.

Stock Options. Under the Plans, the stock option exercise price may not be less than 100% of the fair market value of our common stock on the date of grant. The maximum term of any stock option granted under the 2006 Equity Compensation Plan may not exceed seven years from the date of grant, and those stock options will be exercisable at such times and under conditions as determined by the Compensation Committee of our Board of Directors, subject to the limitations contained in the plan.

Under the 1999 Directors Stock Plan, the stock options granted typically vested and became exercisable on the first anniversary of the grant. The maximum term of any stock option granted under the 1999 Directors Stock Plan was: (a) 10 years from the date of grant for any stock options granted prior to January 25, 2005; and (b) seven years from the date of grant for any stock options granted on or after January 25, 2005.

Under the 1997 Stock Plan, the stock options granted typically vested and became exercisable in three equal annual installments commencing with the first anniversary of the date of grant. The maximum term of any stock option granted under the 1997 Stock Plan was 10 years and two days from the date of grant.

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

	Year Ended December 31, 2010				
	# of Shares	**Weighted Average Exercise Price**	**Aggregate Exercise Price**	**Weighted Average Remaining Contractual Term**	**Aggregate Intrinsic Value (1)**
Outstanding at beginning of period	1,605,806	$67.31	$108,094		
Granted	305,000	$113.41	34,590		
Forfeited	(335)	$35.93	(12)		
Exercised	(179,079)	$44.08	(7,893)		
Expired	(6,601)	$50.30	(332)		
Outstanding at end of period	1,724,791	$77.95	$134,447	4.2 years	$0
Exercisable at end of period	1,193,933	$62.36	$74,457	3.2 years	$1,584

(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 December 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:

	Year Ended December 31,		
	2010	2009	2008
Shares subject to stock options granted	305,000	258,000	177,543
Weighted average grant date fair value	$43.59	$54.05	$36.83
Shares subject to stock options exercised	179,079	210,044	75,435
Intrinsic value of stock options exercised	$8,920	$14,626	$3,165
Proceeds received from stock options exercised	$7,893	$8,800	$3,241
Tax benefits realized from stock options exercised	$3,385	$5,475	$1,201

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:

	Year Ended December 31,		
	2010	2009	2008
Risk-free interest rates	2.2 %	1.6%	2.7%
Expected lives (in years)	4.6	4.5	4.0
Volatility	43%	54%	53%
Dividend yield	None	None	None

Restricted Stock and RSUs. Under the 1997 Stock Plan, restricted shares awarded were subject to a restriction period set by the Compensation Committee of our Board of Directors, during which time the shares may not be sold, transferred, assigned or pledged. For restricted stock awards issued under the 1997 Stock Plan, the restriction period ended on the third anniversary of the date of grant. Under the 2006 Equity Compensation Plan, restricted shares and RSUs awarded are subject to a restriction period of at least: (a) for awards made prior to November 24, 2010, three years in the case of a time-based period of restriction and one year in the case of a performance-based period of restriction; and (b) for awards made after November 24, 2010, one year. All restricted shares and RSUs awarded under the 2006 Equity Compensation Plan as of December 31, 2010 have a time-based restriction period that ends on the third anniversary of the date of grant, except for one grant of 18,249 RSUs made in 2007 which has a time-based restriction period that ends on the fifth anniversary of the date of grant.

The following table sets forth the number of RSUs that were granted, forfeited and vested in the period indicated:

	Year Ended December 31, 2010	
	# of RSUs	Weighted Average Grant Date Fair Value
Unvested at beginning of period	125,550	$92.31
Granted	47,676	$108.78
Forfeited	(9,374)	$106.68
Vested	(35,049)	$85.51
Unvested at end of period	128,803	$99.22

The total fair market value of the RSUs vested during the year ended December 31, 2010 was $3,593.

4. Stock Repurchases

As of December 31, 2010, 4,836,725 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:

	Year Ended December 31,	
	2010	**2009**
Number of shares	5,657,500	3,477,875
Total cost	$434,656	$348,123
Average price per share	$76.83	$100.10

From January 31, 2011 through February 14, 2011, we repurchased 1,050,000 outstanding shares of our common stock pursuant to our existing repurchase authorization at a total cost of $69,920 or at an average cost per share of $66.59.

5. Debt

We were a party to an Amended and Restated Credit Agreement dated December 17, 2007 and amended as of March 19, 2009 (the "Prior Credit Agreement") with a single lender to borrow up to $160,000 under two revolving credit facilities: one in the maximum principal amount of $50,000; and the other in the maximum principal amount of $110,000. The borrowings under each credit facility could have been secured or unsecured at our election, provided that we had not defaulted under the Prior Credit Agreement.

Borrowings under the Prior Credit Agreement bore interest at the London Interbank Offered Rate (the "LIBOR"), plus an applicable margin based on our indebtedness to net worth ratio, adjusted quarterly. We paid a commitment fee of 0.15% per annum of the average daily unused amount of the credit facilities

We entered into a Second Amended and Restated Credit Agreement dated as of January 11, 2010 and amended as of February 3, 2010 and August 10, 2010 with two unaffiliated lenders (the "Restated Credit Agreement") which amends and restates in its entirety the Prior Credit Agreement. The Restated Credit Agreement provides for two lines of credit, one in the maximum principal amount of $100,000, and the other in the maximum principal amount of $50,000. Both lines of credit mature on May 1, 2012. The $150,000 of borrowings outstanding under the Prior Credit Agreement continued as borrowings under the Restated Credit Agreement. Borrowings under the Restated Credit Agreement have been and may be used to allow us to continue repurchasing shares of our common stock while maintaining compliance with certain financial ratios required by various education authorities that regulate us.

Borrowings under the Restated Credit Agreement bear interest, at our option, at LIBOR plus an applicable margin or at an alternative base rate, as defined under the Restated Credit Agreement. We pay a facility fee under the Restated Credit Agreement equal to 0.30% per annum on the daily amount of the commitment of each lender (whether used or unused). As of December 31, 2010, the borrowings under the Restated Credit Agreement were $150,000, all of which were secured, and bore interest at a rate of 0.79% per annum. Approximately $157,950 of our investments and cash equivalents held in a pledged account served as collateral for the secured borrowings as of December 31, 2010.

The borrowings under each line of credit may be secured or unsecured at our election except if an event that would be a default under the Restated 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 Restated Credit Agreement. Secured borrowings may not exceed 95% of the fair market value of the collateral.

The Restated Credit Agreement contains, among other things, covenants, representations and warranties and events of default customary for credit facilities. Our material subsidiaries also guarantee the obligations under the Restated Credit Agreement. The availability of borrowings under the Restated Credit Agreement is subject to our ability at the time of borrowing to satisfy certain specified conditions. We are required to maintain:

- a certain maximum leverage ratio at the end of each of our fiscal quarters;
- a quarterly minimum ratio of cash and investments to indebtedness; and
- a minimum United States Department of Education ("ED") financial responsibility composite ratio as of the end of each fiscal year.

We were in compliance with those requirements as of December 31, 2010.

We recognized interest expense on our borrowings of $1,912 in the year ended December 31, 2010, $717 in the year ended December 31, 2009 and $4,559 in the year ended December 31, 2008.

6. Financial Aid Programs

We participate in various Title IV Programs of the HEA. In 2010, approximately 59% of our revenue determined on a cash accounting basis under the calculation of the provision of the HEA commonly referred to as the "90/10 Rule" was from funds distributed under these programs.

We administer the Title IV Programs in separate accounts as required by government regulation. We are required to administer the funds in accordance with the requirements of the HEA and the ED's regulations and must use due diligence in approving and disbursing funds and servicing loans. In the event we do not comply with federal requirements, or if student loan default rates rise to a level considered excessive by the federal government, we could lose our eligibility to participate in Title IV Programs or could be required to repay funds determined to have been improperly disbursed. Our management believes that we are in substantial compliance with the federal requirements.

7. Investments

Our available-for-sale investments were classified as short-term investments on our December 31, 2010 and 2009 Consolidated Balance Sheets. 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:					
	December 31, 2010			December 31, 2009		
	Aggregate Fair Value	Amortized Cost	Net Unrealized Gains (Losses)	Aggregate Fair Value	Amortized Cost	Net Unrealized Gains (Losses)
Available-for-Sale Investments:						
Government obligations	$110,560	$110,550	$10	$81,591	$81,634	(43)
Government agency obligations	24,394	24,399	(5)	27,932	27,969	(37)
Corporate obligations	8,903	8,908	(5)	28,747	28,690	57
	$143,857	$143,857	$0	$138,270	$138,293	($23)

We also held a certificate of deposit with a total principal value of $5,303 as of December 31, 2010 and $5,137 as of December 31, 2009. This investment is included in short-term investments on our Consolidated Balance Sheet. All of our debt securities classified as available-for-sale as of December 31, 2010 had contractual maturities within five years.

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:

	Year Ended December 31,		
	2010	2009	2008
Unrealized gains	$104	$0	$428
Unrealized losses	$0	($451)	$0

No unrealized gains or losses were reclassified out of our accumulated other comprehensive income (loss) during our fiscal years ended December 31, 2010 and 2009. We recognized $96 of investment gains in our Consolidated Statement of Income for the year ended December 31, 2010.

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

	Year Ended December 31,		
	2010	2009	2008
Realized gains on the sale of investments	$96	$177	$0
Interest income on investments	731	3,114	6,498
	$827	$3,291	$6,498

8. Property and Equipment

The following table sets forth our property and equipment, net, as of the dates indicated:

	As of December 31,	
	2010	2009
Furniture and equipment	$153,014	$139,982
Buildings and building improvements	126,898	122,270
Land and land improvements	39,598	39,613
Leasehold improvements	16,547	14,000
Software	8,620	8,620
Construction in progress	4,043	1,987
	348,720	326,472
Less: Accumulated depreciation and amortization	(150,507)	(131,023)
Property and equipment, net	$198,213	$195,449

Software includes purchased and internally developed software.

The following table sets forth the depreciation and amortization expense in the periods indicated:

	Year Ended December 31,		
	2010	2009	2008
Depreciation and amortization expense	$26,764	$24,895	$22,230

9. Variable Interests

On January 20, 2010, we entered into agreements with unrelated third parties to establish the PEAKS Private Student Loan Program ("PEAKS Program"), which is a private education loan program for our students. Under the PEAKS Program, an unaffiliated lender makes private education loans to our eligible students and, subsequently, sells those loans to an unaffiliated trust that purchases, owns and collects private education loans ("PEAKS Trust"). The PEAKS Trust issued senior debt in the aggregate principal amount of $300,000 ("PEAKS Senior Debt") to investors. The lender disburses the proceeds of the private education loans to us for application to the students' account balances with us that represent their unpaid education costs. We transfer a portion of the amount of each private education loan disbursed to us under the PEAKS Program to the PEAKS Trust in exchange for a subordinated note issued by the PEAKS Trust ("Subordinated Note").

The Subordinated Note is non-interest bearing and has been recorded net of an unamortized discount based on an imputed interest rate of 9.0% in Other assets on our Condensed Consolidated Balance Sheet. The discount will be amortized over the term of the Subordinated Note, which is expected to be approximately 15 years. The face value of the Subordinated Note as of December 31, 2010 was approximately $62,355.

The PEAKS Trust utilizes the proceeds from the issuance of the PEAKS Senior Debt and the Subordinated Note to purchase the private education loans made by the lender to our students. The assets of the PEAKS Trust (which include, among other assets, the private education loans owned by the PEAKS Trust) serve as collateral for, and are intended to be the principal source of, the repayment of the PEAKS Senior Debt and the Subordinated Note. We guarantee payment of the principal, interest and certain call premiums owed on the PEAKS Senior Debt, and the administrative fees and expenses of the PEAKS Trust ("PEAKS Guarantee"). See Note 13 – Guarantees, for further discussion of the PEAKS Guarantee.

We did not explicitly or implicitly provide any financial or other support to the PEAKS Trust during the fiscal year ended December 31, 2010 that we were not contractually required to provide, and we do not intend to provide any such support to the PEAKS Trust in the foreseeable future, other than what we are contractually required to provide.

The PEAKS Trust is a variable interest entity as defined under ASC 810. We held variable interests in the PEAKS Trust as of December 31, 2010 as a result of the Subordinated Note and PEAKS Guarantee. To determine whether we were the primary beneficiary of the PEAKS Trust, we:

- assessed the risks that the PEAKS Trust was designed to create and pass through to its variable interest holders;
- identified the variable interests in the PEAKS Trust;
- identified the other variable interest holders and their involvement in the activities of the PEAKS Trust;
- identified the activities that most significantly impact the PEAKS Trust's economic performance;
- determined whether we have the power to direct those activities; and
- determined whether we have the right to receive the benefits from, or the obligation to absorb the losses of, the PEAKS Trust that could potentially be significant to the PEAKS Trust.

We determined that the activities of the PEAKS Trust that most significantly impact the economic performance of the PEAKS Trust involve:

- establishing the underwriting criteria of, and the interest rates and fees charged on, the private education loans acquired by the PEAKS Trust; and
- the servicing (which includes the collection) of the private education loans owned by the PEAKS Trust.

To make that determination, we analyzed various possible scenarios of student loan portfolio performance to evaluate the potential economic impact on the PEAKS Trust. In our analysis, we made what we believe are conservative assumptions based on historical data for the following key variables:

- the composition of the credit profiles of the borrowers;
- the interest rates and fees charged on the loans;
- the default rates and the timing of defaults associated with similar types of loans; and
- the prepayment and the speed of repayment associated with similar types of loans.

Based on our analysis, we concluded that we are not the primary beneficiary of the PEAKS Trust, because we do not have the power to direct the activities that most significantly impact the economic performance of the PEAKS Trust. As a result, we are not required under ASC 810 to include the financial results of the PEAKS Trust in our consolidated financial statements for the fiscal year ended December 31, 2010. Our conclusion that we are not the primary beneficiary of the PEAKS Trust did not change from the prior reporting period. Therefore, there was no effect on our consolidated financial statements.

On February 20, 2009, we entered into agreements with an unaffiliated entity (the "2009 Entity") to create a program that makes private education loans available 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 "2009 Loan Program"). Under the 2009 Loan Program, an unaffiliated lender makes private education loans to our eligible students and, subsequently, sells those loans to the 2009 Entity. The 2009 Entity purchases the private education loans from the lender utilizing funds received from its owners in exchange for participation interests in the private education loans acquired by the 2009 Entity. The lender disburses the proceeds of the private education loans to us for application to the students' account balances with us that represent their unpaid education costs.

In connection with the 2009 Loan Program, we entered into a risk sharing agreement (the "2009 RSA") with the 2009 Entity 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 2009 Loan Program, based on the annual dollar volume. See Note 13 – Guarantees, for further discussion of the 2009 RSA.

In addition, we have made advances to the 2009 Entity under a revolving promissory note (the "Revolving Note"). We provided advances of $6,311in the fiscal year ended December 31, 2010 and $18,226 in the fiscal year ended December 31, 2009 to the 2009 Entity under the Revolving Note that we were not contractually required to provide. In the fiscal year ended December 31, 2010, the amount of repayments made by the 2009 Entity to us under the Revolving Note exceeded the amount of our advances to the 2009 Entity under the Revolving Note by $2,982. In the fiscal year ended December 31, 2009, the amount of our advances to the 2009 Entity under the Revolving Note exceeded the amount of repayments made by the 2009 Entity to us under the Revolving Note by $12,851. Substantially all of the assets of the 2009 Entity serve as collateral for the Revolving Note. The Revolving Note bears interest, is subject to customary terms and conditions and may be repaid at any time without penalty prior to its 2025 maturity date.

The advances under the Revolving Note were primarily used by the 2009 Entity to purchase additional private education loans under the 2009 Loan Program. We made the advances instead of retaining the funds and providing internal student financing, which is non-interest bearing. We have no immediate plans to significantly increase the amount of advances that we make to the 2009 Entity under the Revolving Note, but we may decide to do so in the future.

The 2009 Entity is a variable interest entity as defined under ASC 810. We held variable interests in the 2009 Entity as of December 31, 2010 as a result of the Revolving Note and 2009 RSA. To determine whether we were the primary beneficiary of the 2009 Entity, we:

- assessed the risks that the 2009 Entity was designed to create and pass through to its variable interest holders;
- identified the variable interests in the 2009 Entity;
- identified the other variable interest holders and their involvement in the activities of the 2009 Entity;
- identified the activities that most significantly impact the 2009 Entity's economic performance;
- determined whether we have the power to direct those activities; and
- determined whether we have the right to receive the benefits from, or the obligation to absorb the losses of, the 2009 Entity that could potentially be significant to the 2009 Entity.

To identify the activities of the 2009 Entity that most significantly impact the economic performance of the 2009 Entity, we analyzed various possible scenarios of private education loan portfolio performance. In our analysis, we made what we believe are conservative assumptions based on historical data for the following key variables:

- the composition of the credit profiles of the borrowers;
- the interest rates and fees charged on the loans;
- the default rates and the timing of defaults associated with similar types of loans; and
- the prepayment and the speed of repayment associated with similar types of loans.

We determined that the activities of the 2009 Entity that most significantly impact its economic performance involve:

- establishing the underwriting criteria of, and the interest rates and fees charged on, the private education loans acquired by the 2009 Entity; and
- the servicing (which includes the collection) of the private education loans owned by the 2009 Entity.

Based on our analysis, we concluded that we are not the primary beneficiary of the 2009 Entity, because we do not direct those activities. As a result, we are not required under ASC 810 to include the financial results of the 2009 Entity in our consolidated financial statements for the fiscal year ended December 31, 2010. Our conclusion that we are not the primary beneficiary of the 2009 Entity did not change from the prior reporting period. Therefore, there was no effect on our consolidated financial statements.

The carrying value of the Subordinated Note and the Revolving Note as of December 31, 2010 was $18,245 and is included in other assets on our Consolidated Balance Sheet.

10. Income Taxes

The following table sets forth the components of the provision for income taxes in the periods indicated:

	Year Ended December 31,		
	2010	**2009**	**2008**
Current income tax expense:			
U.S. federal	$216,839	$165,806	$116,016
State and local	37,687	28,354	19,227
Total	$254,526	$194,160	$135,243
Deferred income tax expense (benefit):			
U.S. federal	(12,244)	(2,579)	(7,898)
State and local	(2,313)	(487)	(1,491)
Total	(14,557)	(3,066)	(9,389)
Total provision for income taxes	$239,969	$191,094	$125,854

The following table sets forth the components of our deferred income tax assets (liabilities) as of the dates indicated:

	As of December 31,	
	2010	2009
Deferral of book costs	($2,226)	($2,259)
Property and equipment	(2,885)	(5,257)
Pension	(4,465)	(1,187)
Other	(1,230)	(1,947)
Gross deferred tax (liabilities)	($10,806)	($10,650)
Deferred revenue	3,542	3,426
Accounts receivable	2,938	9,846
Legal accrual	2,111	1,486
Compensation and benefits	3,284	1,904
Stock-based compensation	15,113	10,129
Operating leases	1,426	1,952
Other assets	8,885	0
Other	4,400	2,122
Gross deferred tax assets	$41,699	$30,865
Net deferred income tax asset	$30,893	$20,215

The difference between the U.S. federal statutory income tax rate and our effective income tax rate as a percentage of income in the periods indicated is reconciled in the following table:

	Year Ended December 31,		
	2010	2009	2008
U.S. federal statutory income tax rate	35.0%	35.0%	35.0%
State income taxes, net of federal benefit	3.6%	3.6%	3.6%
Other	0.5%	0.3%	(0.2%)
Effective income tax rate	39.1%	38.9%	38.4%

The following table sets forth the activity with respect to our unrecognized tax benefits in the period indicated:

	Year Ended December 31,		
	2010	2009	2008
Balance as of January 1	$13,274	$10,889	$8,564
Increases (decreases) from:			
Tax positions taken during a prior period	522	0	0
Tax positions taken during the current period	9,461	3,053	2,851
Settlements with taxing authorities	(78)	(505)	0
Lapse of statute of limitations	(291)	(163)	(526)
Balance as of December 31	$22,888	$13,274	$10,889

The amount of unrecognized tax benefits that, if recognized, would have affected our effective tax rate as of December 31, 2010 was $12,824. We do not expect the amount of our unrecognized tax benefits to significantly increase or decrease during the next 12 months. The amount of interest and penalties related to unrecognized tax benefits accrued on our Consolidated Balance Sheets was $2,797 as of December 31, 2010 and $961 as of December 31, 2009. In each of the years ended December 31, 2010, 2009 and 2008, the amount of interest expense and penalties related to our unrecognized tax benefits that we recognized in our Consolidated Statement of Income was not material.

We file income tax returns in the United States (federal) and in various state and local jurisdictions. As of December 31, 2010, we were no longer subject to federal, state or local income tax examinations for tax years prior to 2007, except in 12 states where we are still subject to income tax examinations for tax years 2001 through 2006.

11. Employee Benefit Plans

Employee Pension Benefits. Our ESI Pension Plan, a non-contributory defined benefit pension plan, commonly referred to as a cash balance plan, covers substantially all of our employees who began their employment with us prior to June 2, 2003. This plan provides benefits based on an employee's annual earnings times an established percentage of pay determined by the employee's age and years of benefit service. Effective June 2, 2003, we closed participation in the ESI Pension Plan to all new employees. Employees who begin their employment with us on or after June 2, 2003 do not participate in the ESI Pension Plan.

Our ESI Excess Pension Plan, a nonqualified, unfunded retirement plan, covers a select group of our management. The purpose of the ESI Excess Pension Plan is to restore benefits earned, but not available, to eligible

employees under the ESI Pension Plan due to federal statutory limitations on the amount of benefits that can be paid and compensation that may be recognized under a tax-qualified retirement plan.

The benefit accruals under the ESI Pension Plan and the ESI Excess Pension Plan for all participants in those plans were frozen effective March 31, 2006, such that no further benefits accrue under those plans after March 31, 2006. Participants in those plans, however, continue to be credited with vesting service and interest according to the terms of the ESI Pension Plan and the ESI Excess Pension Plan.

Effective January 1, 2011, we changed the rates at which interest is credited under the ESI Pension Plan and ESI Excess Pension Plan. This change resulted in the recognition of $6,322, net of tax, of prior service credits in accumulated other comprehensive loss on our Consolidated Balance Sheet as of December 31, 2010.

The information presented below is based on an actuarial valuation date as of December 31 for 2010 and 2009.

The following table sets forth the change in projected benefit obligation for the periods indicated:

	Year Ended December 31,	
	2010	**2009**
Projected benefit obligation at beginning of year	$53,854	$51,308
Service cost	0	0
Actuarial loss	6,406	2,975
Interest cost	3,048	3,104
Benefits paid	(3,060)	(3,533)
Plan amendments	(10,370)	--
Projected benefit obligation at end of year	$49,878	$53,854
Fair value of plan assets at end of year	61,385	56,966
Funded status at end of year	$11,507	$3,112

Our accumulated benefit obligation was $49,878 at December 31, 2010 and $53,854 at December 31, 2009.

The following table sets forth the funded status of our defined benefit plans that was recognized on our Consolidated Balance Sheets as of the dates indicated:

	As of December 31,	
	2010	**2009**
Non-current assets	$11,752	$3,384
Current (liabilities)	0	0
Non-current (liabilities)	(245)	(272)
Total	$11,507	$3,112

The weighted-average assumptions used to determine benefit obligations as of December 31, 2010 and 2009 are as follows:

	2010	**2009**
Discount rate	5.00%	5.50%
Rate of compensation increase	N/A	N/A

The following table sets forth the change in plan assets for the periods indicated:

	Year Ended December 31,	
	2010	**2009**
Fair value of plan assets at beginning of year	$56,966	$49,458
Actual return on plan assets	7,479	10,513
Employer contributions	0	528
Benefits paid	(3,060)	(3,533)
Fair value of plan assets at end of year	$61,385	$56,966

The following tables set forth the fair value of total plan assets by major asset category as of the dates indicated:

		Fair Value Measurements as of December 31, 2010		
Asset Category	**Total**	**(Level 1) Quoted Prices in Active Markets for Identical Assets**	**(Level 2) Significant Other Observable Inputs**	**(Level 3) Significant Unobservable Inputs**
Cash and cash equivalents	$292	$292	$0	$0
Fixed income securities (a)	20,781	20,781	0	0
Equity securities:				
Domestic large cap	26,322	26,322	0	0
Mid cap value/growth (a)	7,885	7,885	0	0
Small cap value/growth (a)	4,495	4,495	0	0
Foreign equities	1,610	1,610	0	0
Total	$ 61,385	$ 61,385	$0	$0

(a) Mutual funds.

		Fair Value Measurements as of December 31, 2009		
Asset Category	**Total**	**(Level 1) Quoted Prices in Active Markets for Identical Assets**	**(Level 2) Significant Other Observable Inputs**	**(Level 3) Significant Unobservable Inputs**
Cash and cash equivalents	$361	$361	$0	$0
Fixed income securities (a)	22,483	22,483	0	0
Equity securities:				
Domestic large cap	23,519	23,519	0	0
Mid cap value/growth (a)	6,337	6,337	0	0
Small cap value/growth (a)	3,450	3,450	0	0
Foreign equities	73	73	0	0
Preferred stock	743	743	0	0
Total	$56,966	$56,966	$0	$0

(a) Mutual funds.

We used quoted prices in active markets for identical assets as of the measurement dates to value our plan assets that were categorized as Level 1.

The following table sets forth the amounts in accumulated other comprehensive loss on our Consolidated Balance Sheets that have not been recognized as components of net periodic benefit cost as of the dates indicated:

	As of December 31,	
	2010	**2009**
Net actuarial (loss)	($17,824)	($16,413)
Prior service (cost) credit	10,242	(156)
Income tax benefit	2,992	6,499
Total accumulated other comprehensive (loss)	($4,590)	($10,070)

The following table sets forth the components of net periodic pension cost (benefit) in the periods indicated:

	Year Ended December 31,		
	2010	2009	2008
Interest cost	$3,048	$3,103	$3,088
Expected return on assets	(4,401)	(3,819)	(5,228)
Recognized net actuarial loss	1,917	2,364	0
Amortization of prior service cost	28	28	27
Net periodic benefit cost (benefit)	$592	$1,676	($2,113)
Settlement loss	0	46	1,527
Total net periodic pension cost (benefit)	$592	$1,722	($586)

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.

The following table sets forth the amounts related to changes in plan assets and projected benefit obligations that were recognized in other comprehensive (income) loss in the periods indicated:

	Year Ended December 31,		
	2010	2009	2008
Net actuarial (gain) loss	$3,328	($3,765)	$16,922
Amortization of net actuarial loss	(1,917)	(2,364)	0
Prior service cost (credit)	(10,370)	0	184
Amortization of prior service cost	(28)	(28)	0
Other comprehensive (income) loss	($8,987)	($6,157)	$17,106
Total recognized in net periodic pension cost (benefit) and other comprehensive loss (income)	($8,395)	($4,435)	$16,520

The amortization of any prior service cost is determined using a straight-line amortization of the cost over the average remaining service period for employees expected to receive benefits under the pension plans. The estimated net actuarial loss that is expected to be amortized from accumulated other comprehensive loss and recognized in net periodic pension cost for the year ended December 31, 2011 is $1,715 and the estimated prior service credit that is expected to be amortized from accumulated other comprehensive loss and recognized in net periodic pension benefit for the year ended December 31, 2011 is $1,505.

The weighted-average assumptions used to determine net periodic pension cost in the years ended December 31, 2010, 2009 and 2008 are as follows:

	2010	2009	2008
Discount rate	5.50%	6.25%	6.00%
Expected long-term return on plan assets	8.00%	8.00%	8.00%
Rate of compensation increase	N/A	N/A	N/A

The following table sets forth the benefit payments that we expect to pay from the pension plans in the periods indicated:

Year	Amount
Fiscal 2011	$3,342
Fiscal 2012	$3,676
Fiscal 2013	$3,709
Fiscal 2014	$4,353
Fiscal 2015	$3,352
Fiscal 2016 – 2020	$18,792

We invest plan assets based on a total return on investment approach, pursuant to which the plan assets include a diversified blend of equity and fixed income investments toward a goal of maximizing the long-term rate of return without assuming an unreasonable level of investment risk. We determine the level of risk based on an analysis of plan liabilities, the extent to which the value of the plan assets satisfies the plan liabilities and our financial condition. Our investment policy includes target allocations ranging from 30% to 70% for equity investments, 20% to 60% for fixed income investments and 0% to 50% for cash equivalents. The equity portion of the plan assets represents growth and value stocks of small, medium and large companies. We measure and monitor the investment risk of the plan assets both on a quarterly basis and annually when we assess plan liabilities.

We use a building block approach to estimate the long-term rate of return on plan assets. This approach is based on the capital market principle that the greater the volatility, the greater the return over the long term. An analysis of the historical performance of equity and fixed income investments, together with current market factors such as the inflation and interest rates, are used to help us make the assumptions necessary to estimate a long-term rate of return on plan assets. Once this estimate is made, we review the portfolio of plan assets and make adjustments thereto that we believe are necessary to reflect a diversified blend of equity and fixed income investments that is capable of achieving the estimated long-term rate of return without assuming an unreasonable level of investment risk. We also compare the portfolio of plan assets to those of other pension plans to help us assess the suitability and appropriateness of the plan investments.

We determine our discount rate by performing a yield curve analysis based on a portfolio of high-quality fixed income investments with various maturities. Our expected future benefit payments are discounted to their present value at the appropriate yield curve rate to generate the overall discount rate for pension obligations.

In 2010, we made no contributions to the ESI Excess Pension Plan or the ESI Pension Plan. In 2009, we contributed $528 to the ESI Excess Pension Plan and made no contributions to the ESI Pension Plan. We do not expect to make any contributions to either the ESI Pension Plan or the ESI Excess Pension Plan in 2011.

Retirement Savings Plan. Our ESI 401(k) Plan, a defined contribution plan, covers substantially all of our employees. All of our contributions under the ESI 401(k) Plan are in the form of cash to plan investment options directed by the participant.

Our ESI Excess Savings Plan, a nonqualified, unfunded deferred compensation plan, covers a select group of our management. The plan provided for salary deferral of contributions that the participants were unable to make under the ESI 401(k) Plan and our contributions that could not be paid under the ESI 401(k) Plan due to federal statutory limits on the amount that an employee could contribute under a defined contribution plan. Effective for plan years beginning on and after January 1, 2008, we froze the ESI Excess Savings Plan, such that employees may no longer make salary deferrals and we will no longer make contributions under the ESI Excess Savings Plan. Amounts previously credited to an employee under the ESI Excess Savings Plan will, however, continue to accrue interest in accordance with the terms of the ESI Excess Savings Plan until those amounts are distributed pursuant to the plan's terms.

The costs of providing the benefits under the ESI 401(k) Plan and ESI Excess Savings Plan (including certain administrative costs of the plans) were:

- $5,063 in the year ended December 31, 2010;
- $4,430 in the year ended December 31, 2009; and
- $3,043 in the year ended December 31, 2008.

On October 27, 2010, the ED issued a final rule, which goes into effect on July 1, 2011, that prohibits any incentive compensation based directly or indirectly on success in securing enrollments or financial aid to any person or entity engaged in any student recruitment or admission activity or in making decisions regarding the awarding of Title IV Program funds (the "Incentive Compensation Prohibition"). The Incentive Compensation Prohibition precludes profit-sharing payments, but it is not clear whether any of the benefits that we provide under the ESI 401(k) Plan or ESI Excess Savings Plan to our employees would be precluded under the Incentive Compensation Prohibition on and after July 1, 2011.

12. Commitments and 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 December 31, 2010, the total face amount of those surety bonds was approximately $25,993.

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. Although we believe our estimates related to any litigation are reasonable, deviations from our estimates could produce a materially different result. 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. The following is a description of pending litigation that falls outside the scope of litigation incidental to the ordinary course of our business.

On November 3, 2010, a complaint in a securities class action lawsuit was filed against us and two of our current executive officers in the United States District Court for the Southern District of New York under the following caption: *Operating Engineers Construction Industry and Miscellaneous Pension Fund, Individually and On Behalf of All Others Similarly Situated v. ITT Educational Services, Inc., et al.* (the "Operating Engineers Lawsuit"). The complaint alleges, among other things, that the defendants violated Section 10(b) and 20(a) of the Exchange Act and

Rule 10b-5 promulgated thereunder, by making false and misleading statements and engaging in fraudulent business practices. The putative class period in this action is from October 23, 2008 through August 13, 2010. The plaintiff seeks, among other things, the designation of this action as a class action, an award of unspecified damages, interest, costs, attorney's fees, equitable relief and injunctive relief. All of the defendants intend to defend themselves vigorously against the allegations made in the complaint.

On November 12, 2010, a complaint in a shareholder derivative lawsuit was filed against three of our current executive officers and all of our current Directors in the United States District Court for the Southern District of New York under the following caption: *Antonio Cosing, Derivatively and On Behalf of ITT Educational Services, Inc. v. Kevin M. Modany, et al.* (the "Cosing Lawsuit"). The complaint alleges, among other things, that from October 23, 2008 through August 13, 2010, the defendants breached their fiduciary duties to us, abused their ability to control and influence us, grossly mismanaged us, caused us to waste corporate assets and were unjustly enriched, by making false and misleading statements and engaging in fraudulent business practices. The complaint seeks, among other things, unspecified damages, equitable and/or injunctive relief, restitution, disgorgement of profits, benefits and other compensation, an order directing us to reform our corporate governance and internal procedures, costs, disbursements and attorneys' fees. All of the individual defendants intend to defend themselves vigorously against the allegations in the complaint. On December 14, 2010, the Cosing Lawsuit was consolidated into the Operating Engineers Lawsuit.

On November 22, 2010, another complaint in a shareholder derivative lawsuit was filed against seven of our current officers and all of our current Directors in the United States District Court for the Southern District of Indiana under the following caption: *Roger B. Orensteen, derivatively on behalf of ITT Educational Services, Inc. v. Kevin M. Modany, et al.* The complaint alleges, among other things, that, from January 2008 through August 2010, the defendants violated Sections 10(b) and 20(a) of the Exchange Act, breached their fiduciary duties to us, abused their ability to control and influence us, grossly mismanaged us, caused us to waste corporate assets and were unjustly enriched, by making false and misleading statements and engaging in fraudulent business practices. The complaint seeks, among other things, unspecified damages, restitution, disgorgement of profits, benefits and other compensation, an order directing us to reform our corporate governance and internal procedures, costs, disbursements and attorneys' fees. All of the individual defendants intend to defend themselves vigorously against the allegations in the complaint.

On December 3, 2010, another complaint in a shareholder derivative lawsuit was filed against two of our current executive officers and all of our current Directors in the United States District Court for the Southern District of New York under the following caption: *J. Kent Gregory, derivatively on behalf of ITT Educational Services, Inc. v. Kevin M. Modany, et al.* (the "Gregory Lawsuit"). The complaint alleges, among other things, that the defendants breached their fiduciary duties to us, were unjustly enriched by us and misappropriated information about us, by making false and misleading statements and engaging in fraudulent business practices. The complaint seeks, among other things, unspecified damages, restitution, disgorgement of profits, benefits and other compensation, an order directing us to reform our corporate governance and internal procedures, costs, disbursements and attorneys' fees. All of the individual defendants intend to defend themselves vigorously against the allegations in the complaint. The Gregory Lawsuit was consolidated into the Cosing Lawsuit on December 13, 2010 and further consolidated into the Operating Engineers Lawsuit on December 14, 2010.

Lease Commitments. We lease 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 13 years and we expect 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 operating lease terms for taxes, insurance and other operating expenses incurred during the operating lease period.

Rent expense under our operating leases was:

- $43,777 in the year ended December 31, 2010;
- $37,987 in the year ended December 31, 2009; and
- $32,574 in the year ended December 31, 2008.

Future minimum rental payments required under our operating leases that have initial or remaining non-cancelable lease terms in excess of one year as of December 31, 2010 are as follows:

2011	$42,942
2012	43,588
2013	38,269
2014	30,040
2015	17,092
2016 and thereafter	11,629
	$183,560

Future minimum rental payments related to equipment leases are not significant.

13. Guarantees

We entered into the PEAKS Guarantee in connection with the PEAKS Program. Under the PEAKS Guarantee, we guarantee payment of the principal, interest and certain call premiums owed on the PEAKS Senior Debt, and the administrative fees and expenses of the PEAKS Trust. The PEAKS Senior Debt bears interest at a variable rate based on the LIBOR plus an applicable margin and matures in January 2020. The PEAKS 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 PEAKS Senior Debt could require us to purchase their PEAKS Senior Debt in certain limited circumstances that pertain to our continued eligibility to participate in the federal student financial aid programs under 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 PEAKS Senior Debt and the PEAKS 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 the PEAKS Guarantee to the extent that funds are remaining in the PEAKS Trust.

The maximum future payments that we could be required to make under the PEAKS Guarantee include:

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

We are not able to estimate the undiscounted maximum potential amount of future payments that we could be required to make under the PEAKS Guarantee, 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 PEAKS Senior Debt and to pay the fees and expenses of the PEAKS Trust;
- the fact that the interest rate on the PEAKS Senior Debt is a variable rate based on the LIBOR plus a margin;
- whether certain call premiums will be payable in connection with the PEAKS Senior Debt; and
- the amount of fees and expenses of the PEAKS Trust.

We entered into the 2009 RSA in connection with the 2009 Loan Program. Under the 2009 RSA, we have guaranteed the repayment of the principal amount (including capitalized origination fees) and accrued interest payable on any private education loans that are charged off above a certain percentage of the private education loans made under the 2009 Loan Program, based on the annual dollar volume. The total initial principal amount of private education loans that the 2009 Entity is expected to purchase under the 2009 Loan Program is approximately $141,000. Our obligations under the 2009 RSA will remain in effect until all private education loans made under the 2009 Loan Program are paid in full or charged off. The standard repayment term for a private education loan made under the 2009 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 2009 Loan Program. As of December 31, 2010, the total collateral maintained in a restricted bank account was not material. This amount is included in Other assets on our Consolidated Balance Sheet as of December 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 December 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 standard repayment term for a private education loan made under the 2007 RSA is ten years, with repayment generally beginning six months after a student graduates, withdraws or is terminated from his or her program of study.

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 educations 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 December 31, 2010, we had not made any guarantee payments under the PEAKS Guarantee, the 2009 RSA or the 2007 RSA, and our recorded liability for the guarantee obligations related to those arrangements included in other liabilities on our Consolidated Balance Sheet was not material.

Appendix 1

Management's Report on Internal Control Over Financial Reporting

We are responsible for establishing and maintaining adequate internal control over our financial reporting, as defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act ("ICFR"). Our ICFR is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

- pertain to the maintenance of our records that in reasonable detail accurately and fairly reflect our transactions and asset dispositions;
- provide reasonable assurance that our transactions are recorded as necessary to permit the preparation of our financial statements in accordance with generally accepted accounting principles;
- provide reasonable assurance that our receipts and expenditures are being made only in accordance with authorizations of our management and Board of Directors (as appropriate); and
- provide reasonable assurance regarding the prevention or timely detection of any unauthorized acquisition, use or disposition of our assets that could have a material effect on our financial statements.

Reasonable assurance, as defined in Section 13(b)(7) of the Exchange Act, is the level of detail and degree of assurance that would satisfy prudent officials in the conduct of their own affairs in devising and maintaining a system of internal accounting controls.

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

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we assessed the effectiveness of our ICFR as of December 31, 2010. Our assessment included extensive documenting, evaluating and testing of the design and operating effectiveness of our ICFR. In making this assessment, our management used the criteria for Internal Control-Integrated Framework set forth by The Committee of Sponsoring Organizations of the Treadway Commission. These criteria are in the areas of control environment, risk assessment, control activities, information and communication, and monitoring. Based on our assessment using these criteria, our management concluded that we maintained effective ICFR as of December 31, 2010.

The effectiveness of our ICFR as of December 31, 2010 has been audited by PricewaterhouseCoopers LLP, our independent registered public accounting firm, as stated in its accompanying report.