

Education that builds careers.

Atlanta San Diego Charlotte Dallas Ft. Lauderdale Houston
Las Vegas Los Angeles Minneapolis Boston Pittsburgh
Portland Philadelphia Phoenix Seattle San Francisco Denver
Washington, D.C. Chicago Schaumburg New York City Miami
Boston Pittsburgh Portland Philadelphia Phoenix Seattle San
Francisco Denver Washington, D.C. Chicago Schaumburg
New York City Miami Atlanta San Diego Charlotte Dallas Ft.
Lauderdale Houston Las Vegas Los Angeles Minneapolis
Atlanta San Diego Charlotte Dallas Ft. Lauderdale Houston
Las Vegas Los Angeles Minneapolis Boston Pittsburgh
Portland Philadelphia Phoenix Seattle San Francisco Denver
Washington, D.C. Chicago Schaumburg New York City Miami
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Francisco Denver Washington, D.C. Chicago Schaumburg
New York City Miami Atlanta San Diego Charlotte Dallas Ft.
Lauderdale Houston Las Vegas Los Angeles Minneapolis
Atlanta San Diego Charlotte Dallas Ft. Lauderdale Houston

Education Management Corporation

Education Institutions

The Art Institute of Atlanta® (AiA)
The Art Institute of California® (AiCA)
The Art Institute of Charlotte® (AiCH)
The Art Institute of Colorado® (AiC)
The Art Institute of Dallas® (AiD)
The Art Institute of Fort Lauderdale® (AiFL)
The Art Institute of Houston® (AiH)
The Art Institute of Las Vegas® (AiLV)
The Art Institute of Los Angeles® (AiLA)*
The Art Institute of Los Angeles Orange County® (AiLAO)**
The Art Institutes International Minnesota® (AiM)
The Art Institute of Pittsburgh® (AiP)
The Art Institute of Portland® (AiPD)
The Art Institute of Philadelphia® (AiPH)
The Art Institute of Phoenix® (AiPX)**
The Art Institute of Seattle® (AiS)
The Art Institutes International at San FranciscoSM (AiSF)
The Art Institute of Washington® (AiW)***
The Illinois Institute of Art® (ILiC)
The Illinois Institute of Art at Schaumburg® (ILiS)****
International Fine Arts College® (IFAC)
The New England Institute of Art and Communications® (AiNE)
NCPT, Inc.SM
New York Restaurant SchoolSM (NYRS)
The Art Institute OnlineSM (AiO)⁺

* *A branch of The Art Institute of Pittsburgh*

** *A branch of The Art Institute of Colorado*

*** *A branch of The Art Institute of Atlanta*

**** *A branch of The Illinois Institute of Art at Chicago*

+ *The Art Institute Online is a division of The Art Institute of Pittsburgh*

Profile

Education Management Corporation (“EDMC”) is among the largest providers of proprietary postsecondary education in the United States. Through its schools, the Company offers master’s, bachelor’s and associate’s degree programs and nondegree programs. Headquartered in Pittsburgh, Pennsylvania, EDMC employs approximately 3,700 staff and faculty. During fiscal year 2001, fall total enrollment was 28,000 students.

The Art Institutes, EDMC’s largest operating unit, with 23 institutions nationwide, is an important source of design, media arts, fashion, and culinary professionals.

The Company’s Common Stock trades on the Nasdaq National Market under the symbol “EDMC.”

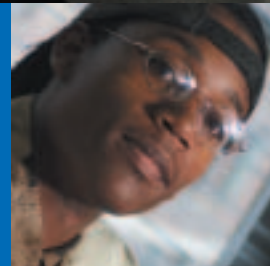
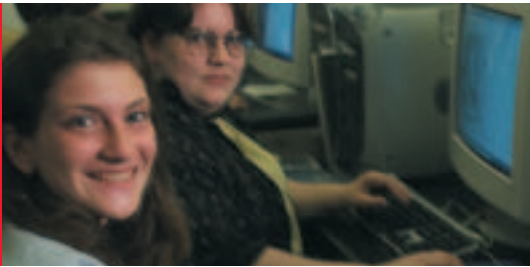
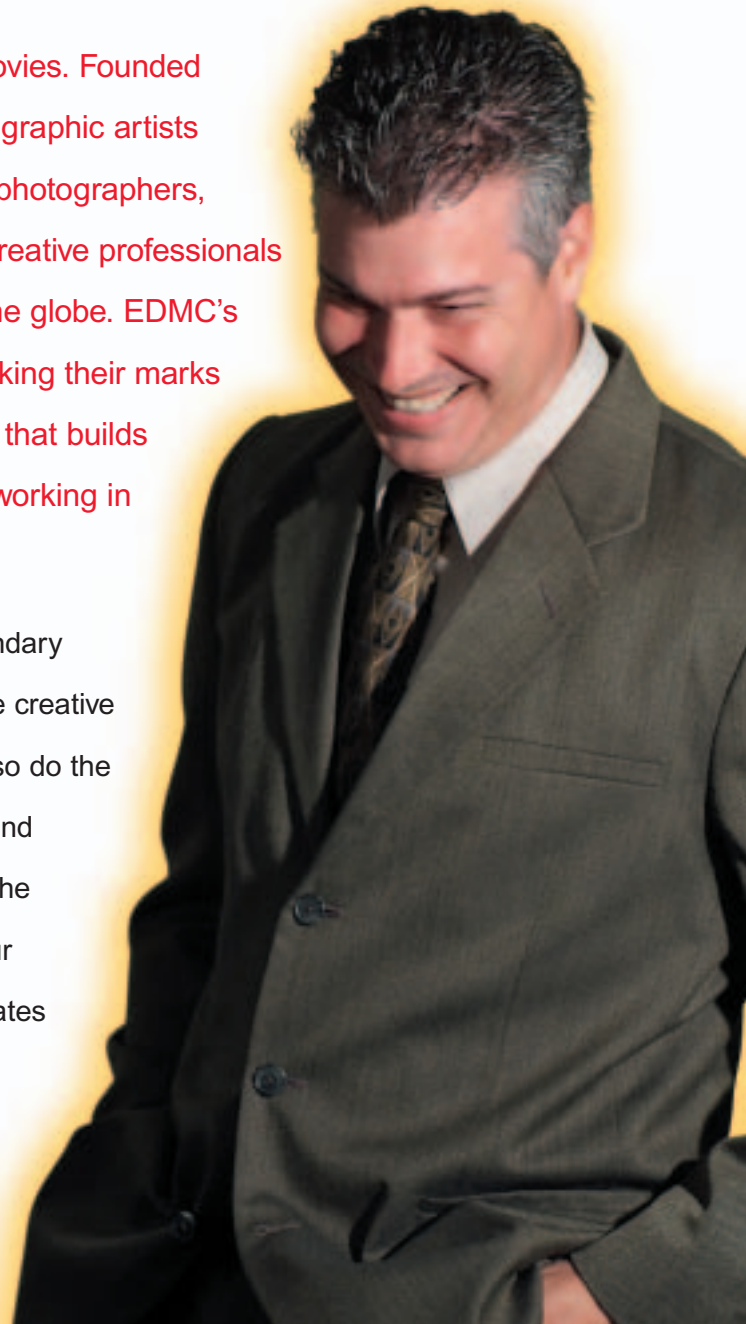
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Education that builds careers.

Our graduates have won Pulitzer Prizes. Made movies. Founded companies. Designed best-selling products. From graphic artists and interior designers to animators, webmasters, photographers, filmmakers, industrial designers and culinarians, creative professionals are critical to the success of companies all over the globe. EDMC's schools have helped mold individuals who are making their marks on industries of every kind. We provide education that builds careers, with 90 percent of our recent graduates working in their fields.

EDMC's Art Institutes, a national system of postsecondary education institutions, is renowned for programs in the creative and applied arts. As industry and technology evolve, so do the education programs we offer. We're market-oriented and constantly seeking to identify the emerging needs of the businesses we serve. Then refining and refocusing our education programs to meet them. It's why our graduates succeed in employment environments that demand creative thinking, teamwork and leadership skills. And when our graduates succeed, so do the businesses that employ them.





The Art Institutes...America's Leader in Creative Education

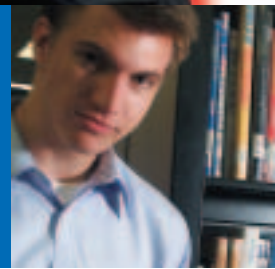
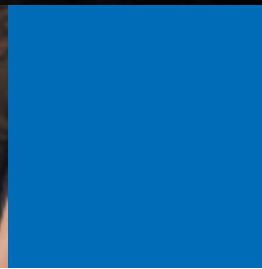
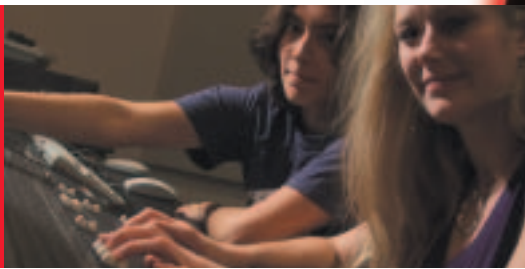
The art of business. The business of art. At The Art Institutes, we help creative individuals develop their talents and prepare to enter the evolving world of business. EDMC's 23 Art Institutes across the country had a peak enrollment last fall of nearly 28,000 students. The Art Institutes offer associate's, bachelor's, and master's degree programs and non-degree programs in an array of creative fields.

What makes the Art Institutes different? Lots. Start with the fact that most of our faculty members remain employed in their industries, so students learn from working professionals. Relationships with leading companies such as Hewlett-Packard, Apple, Adobe and Macromedia, and advisory boards of industry representatives help us keep curricula current with the ever-changing needs of the job market. Staff and faculty are focused first and foremost on the success of our students. So many creative people under one roof – it's a unique education environment.



Principal Education Programs

- ▶ Audio Production
- ▶ Computer Animation
- ▶ Culinary Arts
- ▶ Digital Media Production
- ▶ Fashion Design
- ▶ Fashion Marketing
- ▶ Game Art & Design
- ▶ Graphic Design
- ▶ Industrial Design Technology
- ▶ Interior Design
- ▶ Media Arts & Animation
- ▶ Multimedia & Web Design
- ▶ Photography
- ▶ Restaurant & Catering Management
- ▶ Video Production
- ▶ Visual Effects & Motion Graphics





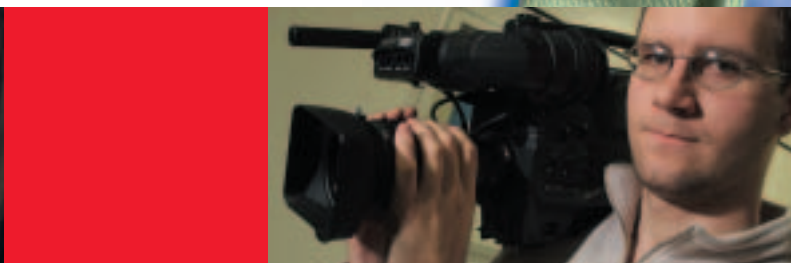
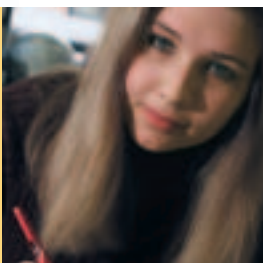
New Developments

In July, we announced the signing of a merger agreement with Argosy Education Group, a Chicago-headquartered organization known principally for its national system of higher education institutions, offering a range of graduate and post-graduate education programs in the fields of psychology, education, business and law, along with undergraduate programs in health care specialties. Over the years, EDMC has entered attractive new education fields or new geographic markets either through start-up or acquisition. The merger with Argosy broadens our presence in the higher education market, and provides a platform to enter more new education disciplines in response to the needs of the economy.

Learn more about EDMC's success

It starts with our basic mission. To take students with raw talent, energy and commitment and to fill them with the knowledge and skills that prepare them to succeed in today's fast-paced economy. Our faculty and staff are committed to this mission.

Visit us at www.edumgt.com for additional information on Education Management Corporation.



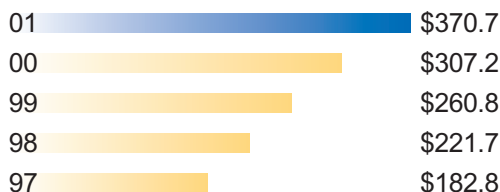
Operating Highlights *for the fiscal years ended June 30*

(Dollars in thousands, except per share amounts)

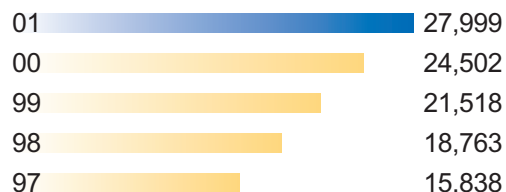
	1999	2000	2001	% change 2000 to 2001
OPERATING RESULTS:				
Net revenues	\$260,805	\$307,249	\$370,681	20.6%
Income before interest and taxes (EBIT)	\$ 31,698	\$ 38,342	\$ 49,675	29.6%
EBIT margin	12.2%	12.5%	13.4%	
Net income	\$ 18,752	\$ 22,530	\$ 28,978	28.6%
Diluted earnings per share	\$.61	\$.75	\$.93	24.0%
BALANCE SHEET DATA:				
Total assets	\$178,746	\$240,675	\$283,946	18.0%
Shareholders' investment	\$ 96,805	\$112,950	\$159,949	41.6%
OTHER SELECTED DATA:				
Capital expenditures ⁽¹⁾	\$ 55,892	\$ 58,149	\$ 38,822	(33.2)%
Schools at end of period	18	20	24	
Student enrollment:				
Beginning of fall quarter	21,518	24,502	27,999	14.3%
Fiscal year average	19,325	22,264	25,549	14.8%

⁽¹⁾ Capital expenditures for fiscal years 1999, 2000 and 2001 reflect approximately \$5.1 million, \$13.2 million and \$4.5 million included in accounts payable at year end, respectively.

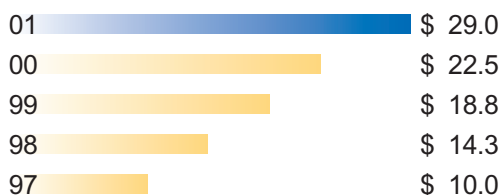
Net Revenues \$ in millions



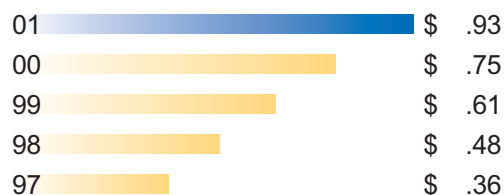
Fall Quarter Beginning Enrollment



Net Income \$ in millions



Earnings Per Share – Diluted



To our shareholders,

Your company enjoyed an outstanding year during fiscal 2001. We continued to execute our growth strategy and took steps to broaden our participation in the higher education market.

The Art Institutes again demonstrated that a focus on student outcomes serves all our constituencies well. Results for our schools' graduates were strong and Education Management delivered record levels of revenues and earnings for the fifth year in a row since becoming publicly traded in 1996.

A greater percentage of our students persisted in their education programs and progressed toward graduation. For the third year in a row, over 90% of our graduates became employed in a field related to their field of study within six months of graduation. In addition, average starting salaries of our graduates over the last three calendar years have grown three times faster than the rate of inflation.

EDMC's consolidated net revenues were \$371 million in the fiscal year ended June 30, 2001, up by more than 20% compared to the prior year.

Student enrollment, measured as of the start of each quarter, grew company-wide by almost 15% year-over-year. Enrollments increased due to growth of our established schools, through the expansion of education program offerings, and through the addition of four new Art Institutes during the year. Net income increased to \$29.0 million in 2001, and earnings per share were up 24% for the year.

We focused our marketing on our web presence and on our high school program. Our representatives visited 12,100 high schools in 2001, compared to 10,300 during the prior year. Inquiries through our web presence have become the second largest source of new students for us. Referrals from students, graduates and employers remain the most important source, representing a third of all new students.



Robert B. Knutson
Chairman and Chief Executive Officer

We got off to a good start in fiscal 2001 with the opening in July of two new Art Institutes: our second Art Institute of Los Angeles in Orange County, and The Art Institute of Washington, located in northern Virginia just across the Potomac River from the District of Columbia. We later acquired The Art Institute of California in San Diego and the Design Institute in Las Vegas, which was renamed The Art Institute of Las Vegas. We are proud to have the faculty and staffs of all four new Art Institutes become a part of our system, and we look forward to serving greater numbers of students and employers in those dynamic metropolitan areas.

In September, 2001, we closed on the acquisition of the International Fine Arts College in Miami, Florida. The acquisition of IFAC represents a continuation of our strategy of

entering attractive new geographic markets and adding promising new education programs. With over 1,000 students, it is our first Art Institute offering a program at the master's degree level. IFAC is well known in South Florida and in Latin America, and we believe that becoming part of The Art Institutes system will help the institution realize its full potential.

Education program introductions have continued to be key drivers of enrollment and revenue growth. During fiscal 2001, our schools introduced over 40 programs that were new to the respective education institution. In response to the needs of employers, most of our new programs are at the bachelor's degree level. Currently, 19 of 23 Art Institutes are eligible to confer baccalaureate degrees, compared to 16 a year ago. During the quarter ended June 30, 2001, bachelor's degree enrollment comprised 33% of our total student body, up from 23% as of a year earlier.

This year, we'll be introducing new bachelor's degree programs titled Visual Effects & Motion Graphics and Digital Media Production, as well as an updated Game Art & Design program. Digital Media Production reflects changing skills and technologies needed for producing content that

can be distributed and displayed in any medium, and Visual Effects & Motion Graphics deals with the design, imaging, layering, and movement of digital elements.

The Art Institute Online and the Center for Professional Development significantly expanded their offerings. AiO is now enrolling students for entirely virtual bachelor's and associate's degree programs in Graphic Design and Multimedia & Web Design, as well as diploma programs in Digital Design and Web Design. Students enrolled at many of the Art Institutes have the option of taking part of their program online through AiO and we expect to be offering the online alternative to all Art Institute students by the end of the current fiscal year.

In July 2001, Education Management and Argosy Education Group announced an agreement to merge. The announcement will lead to the formation of a more comprehensive education enterprise, serving the post-secondary education market from certificate programs through doctoral degrees.

The underlying values of EDMC have been crucial to our success, and I believe those values will serve us well as Argosy is integrated with EDMC. Argosy has a long history of

achievement and their culture has much in common with ours. We have begun extensive planning to facilitate a smooth transition and anticipate receiving regulatory approval prior to the end of the calendar year.

EDMC is known for providing learner-centered education and bringing disciplined planning and execution to all aspects of the business of education. Our culture has enabled us to be successful and we intend to remain true to our values going forward.

At the center of our value system is respect for our students and for the faculty and staff who mentor them. We believe that committed students deserve an attractive return on their economic investment. The satisfaction of our students and their employers is critical to *our* sense of satisfaction, and to the long-term prosperity of our education business. In short, we seek to do the right things the right way.

We're eager to continue to build Education Management Corporation to be the preeminent publicly owned education company.



Robert B. Knutson
Chairman and Chief Executive Officer

Board of Directors

Robert B. Knutson
*Chairman and
Chief Executive Officer
Education Management
Corporation*

Robert H. Atwell
*President Emeritus
American Council on Education*

James J. Burke, Jr.
*Partner
Stonington Partners, Inc.*

William M. Campbell, III
*President
Miramax Television*

Robert P. Gioella
*President and
Chief Operating Officer
Education Management
Corporation*

Albert Greenstone
*President Emeritus
The National Center for
Professional Development*

Miryam L. Knutson
*Former Vice Chairman
Education Management
Corporation*

John R. McKernan, Jr.
*Vice Chairman
Education Management
Corporation*

James S. Pasman, Jr.
*Former President and
Chief Operating Officer
National Intergroup, Inc.
Former Chairman
Permian Oil Corporation*

Executive Officers

Robert B. Knutson
*Chairman and
Chief Executive Officer*

Robert P. Gioella
*President and
Chief Operating Officer*

John R. McKernan, Jr.
Vice Chairman

Robert T. McDowell
*Executive Vice President and
Chief Financial Officer*

David J. Pauldine
President, The Art Institutes

Corporate Offices

300 Sixth Avenue
Pittsburgh, PA 15222-2598

Stock Registrar and Transfer Agent

For address changes, account consolidation, registration changes, lost certificates, and other shareholder services, contact:

Mellon Investor Services
85 Challenger Road
Overpeck Centre
Ridgefield Park, NJ 07660
1-800-756-3353
1-800-231-5469 (for speech and hearing impaired)

Investor Relations

Investor Relations Department
Education Management Corporation
300 Sixth Avenue
Suite 800
Pittsburgh, PA 15222-2598
Phone: (412) 562-0900
Fax: (412) 562-0598
www.artinstitutes.edu
www.edumgt.com

Independent Public Accountants

Arthur Andersen LLP
2100 One PPG Place
Pittsburgh, PA 15222-5498
Phone: (412) 232-0600
Fax: (412) 232-0693

Legal Counsel

Kirkpatrick & Lockhart, LLP
1500 Oliver Building
Pittsburgh, PA 15222-2312
Phone: (412) 355-6500
Fax: (412) 355-6501

Stock Prices and Dividends

The Company's Common Stock is traded on the Nasdaq National Market under the symbol "EDMC." The prices set forth below reflect the high and low sales prices for the Common Stock for the periods indicated, as reported in the consolidated transaction reporting system of the Nasdaq National Market.

Three Months Ended

2001	High	Low
September 30	\$26.94	\$17.75
December 31	38.38	24.75
March 31	37.81	26.06
June 30	40.05	28.92
2000	High	Low
September 30	\$21.13	\$12.38
December 31	14.81	8.69
March 31	14.63	11.00
June 30	18.69	14.88

The Company has not declared or paid any cash dividend on its capital stock during the last two years.

Credits:

Design: Cheryl Bender, Senior Designer, BD&E and
1984 Graduate of the Art Institute of Pittsburgh

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EDMC™

Education Management Corporation

Education that builds careers.

300 Sixth Avenue
Pittsburgh, PA 15222-2598

www.edumgt.com

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended: June 30, 2001

Commission File Number: 000-21363

EDUCATION MANAGEMENT CORPORATION

(Exact name of registrant as specified in its charter)

Pennsylvania

(State or other jurisdiction of
incorporation or organization)

25-1119571

(I.R.S. Employer
Identification No.)

300 Sixth Avenue, Pittsburgh, PA

(Address of principal executive offices)

15222

(Zip Code)

Registrant's telephone number, including area code: **(412) 562-0900**

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

Common Stock, \$.01 par value

(Title of class)

Preferred Share Purchase Rights

(Title of class)

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

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

The aggregate market value of the voting common stock held by non-affiliates of the registrant as of September 11, 2001 was approximately \$531,251,190. The number of shares of Common Stock outstanding on September 11, 2001 was 30,351,322 shares.

Documents incorporated by reference: Portions of the definitive Proxy Statement of the registrant for the annual meeting of shareholders to be held on November 8, 2001 ("Proxy Statement") are incorporated by reference into Part III of this Form 10-K. The incorporation by reference herein of portions of the Proxy Statement shall not be deemed to incorporate by reference the information referred to in Item 402(a)(8) of Regulation S-K.

PART I

Forward-Looking Statements: This Annual Report on Form 10-K contains statements that may be forward-looking statements within the meaning of the U.S. Private Securities Litigation Reform Act of 1995. Those statements can be identified by their use of terms such as “believes,” “estimates,” “anticipates,” “continues,” “contemplates,” “expects,” “may,” “will,” “could,” “should” or “would” or the negatives thereof or other variations thereon or comparable terminology. Those statements are based on the intent, belief or expectation of Education Management Corporation (“EDMC” or the “Company”) as of the date of this Annual Report. Such forward-looking statements are not guarantees of future performance and may involve risks and uncertainties that are outside the control of the Company. Actual results may vary materially from the forward-looking statements contained herein as a result of changes in United States or international economic conditions, governmental regulations and other factors, including those factors described at the end of the response to Item 7 under the heading “Risk Factors.” The Company expressly disclaims any obligation or understanding to release publicly any updates or revisions to any forward-looking statement contained herein to reflect any change in the Company’s expectations with regard thereto or any change in the events, conditions or circumstances on which any such statement is based. The following discussion should be read in conjunction with the Consolidated Financial Statements and Notes thereto filed in response to Item 8 of this Annual Report.

ITEM 1—BUSINESS

Business Overview

EDMC is among the largest providers of proprietary postsecondary education in the United States, based on student enrollment and revenues. The Company was organized as a Pennsylvania corporation in 1962 and completed its initial public offering (the “IPO”) in 1996. Through its main operating unit, the Art Institutes (“The Art Institutes”), the Company offers bachelor’s and associate’s degree programs and non-degree programs in the areas of design, media arts, culinary arts and fashion. The Company’s Art Institutes have graduated over 125,000 students. In the fall quarter beginning October 2000, EDMC’s schools had 27,999 students enrolled, representing all 50 states and 97 countries.

As of June 30, 2001, The Art Institutes consisted of 22 schools in 20 cities throughout the United States. Art Institute programs are designed to provide the knowledge and skills necessary for entry-level employment in various fields, including graphic design, media arts and animation, multimedia and web design, video production, interior design, industrial design, culinary arts, photography, and fashion. These programs typically are completed in 18 to 48 months and culminate in a bachelor’s or associate’s degree. In the summer quarter beginning July 2001, 19 Art Institutes offered bachelor’s degree programs, and EDMC expects to continue to introduce bachelor’s degree programs at schools in states that permit proprietary postsecondary institutions to offer such programs.

The Company offers a culinary arts curriculum at 11 Art Institutes. In addition, The New York Restaurant School (“NYRS”), a culinary arts and restaurant management school located in New York City and owned by the Company, offers an associate’s degree program and certificate programs in these fields.

The Company also owns NCPT (The National Center for Paralegal Training), which offers paralegal certificate programs. The National Center for Professional Development (NCPD) maintained consulting relationships with certain colleges and universities to assist in the development, marketing and delivery of paralegal, legal nurse consultant and financial planning certificate programs. As of June 30, 2001, all but one of these relationships had expired or had been terminated, and the remaining relationship expired on August 31, 2001.

EDMC’s graduates are employed by a broad range of employers nationwide. Approximately 90.7% of the calendar year 2000 graduates of all programs at EDMC’s schools who were available for employment obtained positions in fields related to their programs of study within six months of graduation.

The Business of Education

EDMC's primary mission is to promote student success by providing students with the education necessary to meet employers' current and anticipated needs. To achieve this objective, the Company focuses on marketing to a broad range of potential students, admitting students who possess the relevant interests and capabilities, providing students with programs of study taught by industry professionals, and assisting students with job placement.

Student Recruitment and Marketing

The general reputation of The Art Institutes and referrals from current students, alumni and employers are the largest sources of new students. The Company also employs marketing tools such as the Internet, high school visits and recruitment events, and television and print media advertising. EDMC uses its internal advertising agency to create publications, television and radio commercials, videos and other promotional materials for the Company's schools. The Company estimates that in fiscal 2001 referrals accounted for 34% of new student enrollment at The Art Institutes, high school recruitment programs accounted for 19%, the Company's web sites accounted for 19%, broadcast advertising accounted for 17%, print media accounted for 6%, direct mail efforts accounted for 3%, and international marketing accounted for less than 1%. The remainder was classified as miscellaneous.

In fiscal 2001, The Art Institutes' marketing efforts generated inquiries from approximately 370,000 qualified prospective students. The Art Institutes' inquiry-to-application conversion ratio decreased from 9.7% in fiscal 2000 to 9.1% in fiscal 2001, and the applicant-to-new student ratio was 63.8% for both fiscal 2000 and 2001.

The Company also employs approximately 100 representatives who make presentations at high schools to promote The Art Institutes. Art Institute representatives also participate in college fairs at which prospective students can meet with a representative, view artwork and videos, and receive enrollment information. In fiscal 2001, representatives visited over 12,000 high schools and attended approximately 1,800 career events. Summer teenager and teacher workshops are held to inform students and educators of the education programs offered by The Art Institutes. The Company's marketing efforts to reach young adults and working adults who may be attracted to evening programs are conducted through local newspaper advertising, direct mail campaigns and broadcast advertising.

Student Admissions and Retention

Each applicant for admission to an Art Institute is required to have a high school diploma or a recognized equivalent and to submit a written essay. Prospective students are interviewed to assess their qualifications, their interest in the programs offered by the applicable Art Institute and their commitment to their education. In addition, the curricula, student services, education costs, available financial resources and student housing are reviewed during interviews, and tours of the facilities are conducted for prospective students.

Art Institute students are of varying ages and backgrounds. For fiscal 2001, approximately 31% of the entering students matriculated directly from high school, approximately 29% were between the ages of 19 and 21, approximately 28% were 22 to 29 years of age and approximately 12% were 30 years old or older.

Students at the Company's schools may fail to finish their programs for a variety of personal, financial or academic reasons. To reduce the risk of student withdrawals, each Art Institute devotes staff resources to advising students regarding academic and financial matters, part-time employment and housing. Remedial courses are mandated for students with lower academic skill levels and tutoring is encouraged for students experiencing academic difficulties. The Art Institutes' net annual persistence rate, which measures the number of students who are enrolled during a fiscal year and either graduate or advance to the next fiscal year, was 64.8% in fiscal 2000 and 65.7% in fiscal 2001.

Education Programs

The Art Institutes offer the following degree programs. Not all programs are offered at each Art Institute. (For internal purposes, the Company classifies its degree programs according to four “schools” or areas of study.)

The School of Design

Associate’s Degree Programs

- Computer-Aided Drafting & Design
- Animation Art & Design
- Graphic Design
- Interior Design
- Industrial Design Technology

Bachelor’s Degree Programs

- Media Arts & Animation
- Game Art & Design
- Graphic Design
- Interior Design
- Industrial Design

The School of Culinary Arts

Associate’s Degree Programs

- Culinary Arts
- Restaurant and Catering Management

Bachelor’s Degree Programs

- Culinary Management

The School of Media Arts

Associate’s Degree Programs

- Audio Production
- Broadcasting
- Information Technology & Design
- Photography
- Multimedia & Web Design
- Video Production

Bachelor’s Degree Programs

- Multimedia & Web Design
- Photography

The School of Fashion

Associate’s Degree Programs

- Fashion Design
- Fashion Marketing
- Visual Merchandising

Bachelor’s Degree Programs

- Fashion Design
- Fashion Marketing and Management

NYRS also offers an associate’s degree program in culinary arts and restaurant management and certificate programs in culinary arts, pastry arts, culinary skills and restaurant management.

Approximately 7.9% of the average quarterly student enrollment at the Company’s schools in fiscal 2001 were in specialized diploma and certificate programs. Academic credits from the specialized diploma programs at The Art Institutes and NYRS are generally transferable into bachelor’s and associate’s degree programs at those schools. Diploma and certificate programs are designed for working adults who seek to supplement their education or are interested in enhancing their marketable skills.

During fiscal 2001, The Illinois Institute of Art at Schaumburg, The Art Institute of Colorado and The Art Institute of Houston began offering certificate programs through the Center for Professional Development. The Center for Professional Development was formed to develop and administer certificate programs to a wide audience, including alumni seeking advances in their career fields and professionals in other career fields looking to add marketable new skill sets. Additionally, the Center for Professional Development will conduct contract skills training for companies seeking to update their employees’ skills.

Graduate Employment

Based on information received from graduating students and employers, the Company believes that students graduating from the Company's schools during the five calendar years ended December 31, 2000 obtained employment in fields related to their programs of study as follows:

<u>Graduating Classes (Calendar Year)</u>	<u>Number of Available Graduates(1)</u>	<u>Percentage of Available Graduates Who Obtained Employment Related to Program of Study(2)</u>
2000	5,414	90.7%
1999	5,279	90.1
1998	4,719	90.9
1997	4,749	87.3
1996	4,167	86.4

- (1) The term "Available Graduates" refers to all graduates except those who are pursuing further education, deceased, in active military service, who have medical conditions that prevent such graduates from working, who are continuing in a professional unrelated career, or who are international students no longer residing in the United States.
- (2) The information presented reflects employment in fields related to graduates' programs of study within six months after graduation.

For calendar year 2000, the approximate average starting salaries of graduates of degree and diploma programs at The Art Institutes were as follows: The School of Culinary Arts—\$25,557; The School of Design—\$28,529; The School of Fashion—\$25,861; and The School of Media Arts—\$27,719.

Each Art Institute offers career-planning services to all graduating students through its Career Services department. Specific career advice is provided during the last two quarters of a student's education. In addition to individualized training in interviewing and networking techniques and resume-writing, a Career Development course is required for all students. Students also receive portfolio counseling where appropriate. The Art Institutes maintain contact with approximately 40,000 employers nationwide. Career Services advisors educate employers about the programs at The Art Institutes and the caliber of their graduates. These advisors also participate in professional organizations, trade shows and community events to keep apprised of industry trends and maintain relationships with key employers. Career Services staff also visit employer sites to learn more about their operations and better understand their recruiting needs.

Employers of Art Institute graduates include numerous small and medium-sized companies, as well as larger companies with a national or international presence. The following companies are representative of the larger companies that employ Art Institute graduates: AT&T, Microsoft Corporation, Marriott International, Inc., Home Depot, Viacom, The Gap, Federated Department Stores, The Boeing Company, Eddie Bauer, Inc., Ethan Allen Interiors, Inc., FlightSafety International, Humongous Entertainment, Inc., Kinko's Corporation, Sodexo, The May Department Stores Company, The Neiman Marcus Group, Inc., Aramark, Nintendo of America, Nordstrom, Inc., The Ritz-Carlton, Sears Roebuck and Co., Sierra On-Line, Inc., Starwood Hotels & Resorts, Fox Entertainment Group, TCI International, Inc., Time Warner, Inc., and The Walt Disney Company.

Accreditation

Accreditation is a process through which an institution submits itself to qualitative review by an organization of peer institutions. Accrediting agencies primarily examine the academic quality of the instructional programs of an institution, and a grant of accreditation is generally viewed as certification that an institution's programs meet generally accepted academic standards. Accrediting agencies also review the administrative and financial operations of the institutions they accredit to ensure that each institution has the resources to perform its educational mission.

Pursuant to provisions of the Higher Education Act of 1965, as amended (“HEA”), the U.S. Department of Education relies on accrediting agencies to determine whether institutions’ educational programs qualify them to participate in federal financial aid programs under Title IV of the HEA (“Title IV Programs”). The HEA specifies certain standards that all recognized accrediting agencies must adopt in connection with their review of postsecondary institutions. All of EDMC’s schools are accredited by one or more accrediting agencies recognized by the U.S. Department of Education. Seven of the Company’s schools are accredited by one of the six regional accrediting agencies that accredit virtually all of the public and private non-profit colleges and universities in the United States.

The following table shows the location of each of EDMC’s schools, the name under which it operates, the year of its establishment, the date EDMC opened or acquired it, and the accrediting agency (for schools accredited by more than one recognized accrediting agency, the primary accrediting agency is listed first).

<u>School</u>	<u>Location</u>	<u>Calendar Year Established</u>	<u>Fiscal Year EDMC Acquired/ Opened</u>	<u>Accrediting Agency</u>
The Art Institute of Atlanta	Atlanta, GA	1949	1971	Commission on Colleges of the Southern Association of Colleges and Schools (“SACS”)
The Art Institute of California	San Diego, CA	1981	2001	Accrediting Commission of Career Schools and Colleges of Technology (“ACCSCT”)
The Art Institute of Charlotte	Charlotte, NC	1973	2000	Accrediting Council of Independent Colleges and Schools (“ACICS”)
The Art Institute of Colorado	Denver, CO	1952	1976	ACICS
The Art Institute of Dallas	Dallas, TX	1964	1985	SACS
The Art Institute of Fort Lauderdale	Fort Lauderdale, FL	1968	1974	ACICS
The Art Institute of Houston	Houston, TX	1974	1979	SACS
The Art Institute of Las Vegas	Las Vegas, NV	1983	2001	ACCSCT
The Art Institute of Los Angeles	Los Angeles, CA	1997	1998	ACCSCT & ACICS (as a branch of The Art Institute of Pittsburgh)
The Art Institute of Los Angeles—Orange County	Orange County, CA	2000	2001	ACICS (as a branch of The Art Institute of Colorado)
The Art Institute Online	Pittsburgh, PA	1999	2000	Approved to offer programs as a division of The Art Institute of Pittsburgh
The Art Institute of Philadelphia	Philadelphia, PA	1971	1980	ACICS
The Art Institute of Phoenix	Phoenix, AZ	1995	1996	ACICS (as a branch of The Art Institute of Colorado)
The Art Institute of Pittsburgh	Pittsburgh, PA	1921	1970	ACCSCT, ACICS
The Art Institute of Portland	Portland, OR	1963	1998	Commission on Colleges of the Northwest Association of Schools and Colleges (“NWASC”)
The Art Institutes International at San Francisco	San Francisco, CA	1939	1998	ACICS
The Art Institute of Seattle	Seattle, WA	1946	1982	NWASC
The Art Institute of Washington	Arlington, VA	2000	2001	SACS (as a branch of The Art Institute of Atlanta)
The Art Institutes International Minnesota	Minneapolis, MN	1964	1997	ACICS
The Illinois Institute of Art at Chicago	Chicago, IL	1916	1996	ACCSCT
The Illinois Institute of Art at Schaumburg	Schaumburg, IL	1983	1996	ACCSCT, as a branch of The Illinois Institute of Art at Chicago
Massachusetts Communications College (1)	Boston, MA	1988	2000	New England Association of Schools and Colleges, Inc. through its Commission on Technical and Career Institutions
NCPT: The National Center for Paralegal Training	Atlanta, GA	1973	1973	ACICS
The New York Restaurant School	New York, NY	1980	1997	ACCSCT, ACICS, New York State Board of Regents

(1) Subsequent to June 30, 2001, the school was renamed The New England Institute of Art and Communications.

Accrediting agencies monitor each institution's performance in specific areas. In the event that the information provided by a school to an accrediting agency indicates that such school's performance in one or more areas falls below certain parameters, the accrediting agency may require that school to supply it with supplemental reports on the accrediting agency's specific areas of concern until that school meets the accrediting agency's performance guideline or standard. A school that is subject to this heightened monitoring must seek the prior approval of its accrediting agency in order to open or commence teaching at new locations. The accrediting agencies do not consider requesting that a school provide supplemental reports to be a negative action.

Student Financial Assistance

Many students at EDMC's schools must rely, at least in part, on financial assistance to pay for the cost of their education. The largest source of such support is the federal programs of student financial assistance under Title IV of the Higher Education Act (HEA). Additional sources of funds include other federal grant programs, state grant and loan programs, private loan programs and institutional grants and scholarships. To provide students access to financial assistance resources available through Title IV Programs, a school must be (i) authorized to offer its programs of instruction by the relevant agency of the state in which it is located, (ii) accredited by an agency recognized by the U.S. Department of Education, and (iii) certified as an eligible institution by the U.S. Department of Education. In addition, the school must ensure that Title IV Program funds are properly accounted for and disbursed in the correct amounts to eligible students. All of the Company's schools can participate in Title IV Programs.

Nature of Federal Support for Postsecondary Education

While the states support public colleges and universities primarily through direct state subsidies, the federal government provides a substantial part of its support for postsecondary education in the form of grants and loans to students who can use this support at any institution that has been certified as eligible by the U.S. Department of Education. Students at EDMC's schools receive loans, grants and work-study funding to fund their education under several Title IV Programs, of which the two largest are the Federal Family Education Loan ("FFEL") program and the Federal Pell Grant ("Pell") program. The Company's schools also participate in the Federal Supplemental Educational Opportunity Grant ("FSEOG") program, the Federal Perkins Loan ("Perkins") program, and the Federal Work-Study ("FWS") program.

FFEL. The FFEL program consists of two types of loans: Stafford loans, which are made available to students regardless of financial need, and PLUS loans, which are made available to parents of students classified as dependents. Under the Stafford loan program, a student may borrow up to \$2,625 for the first academic year, \$3,500 for the second academic year and, in certain educational programs, \$5,500 for each of the third and fourth academic years. Students who are classified as independent can obtain an additional \$4,000 for each of the first and second academic years and, depending upon the educational program, an additional \$5,000 for each of the third and fourth academic years. Amounts received by students in the Company's schools under the Stafford loan program in fiscal 2001 equaled approximately 35% of the Company's net revenues. PLUS loans may be obtained by the parents of a dependent student in an amount not to exceed the difference between the total cost of that student's education (including allowable expenses) and other aid to which that student is entitled. Amounts received by parents of students in the Company's schools under the PLUS loan program in fiscal 2001 equaled approximately 16% of the Company's net revenues.

Pell. Pell grants are the primary component of the Title IV Programs under which the U.S. Department of Education makes grants to students who demonstrate financial need. Every eligible student is entitled to receive a Pell grant; there is no institutional allocation or limit. During fiscal 2001, Pell grants ranged up to \$3,300 per year; beginning on July 1, 2001, the limit was increased to \$3,750 per year. Amounts received by students enrolled in the Company's schools in fiscal 2001 under the Pell program represented approximately 6.5% of the Company's net revenues.

FSEOG. FSEOG awards are designed to supplement Pell grants for the neediest students. FSEOG grants generally range in amount from \$300 to \$1,200 per year; however, the availability of FSEOG awards is limited by the amount of those funds allocated to an institution under a formula that takes into account the size of the institution, its costs and the income levels of its students. The Company is required to make a 25% matching contribution for all FSEOG program funds disbursed. Resources for this institutional contribution may include institutional grants and scholarships and, in certain states, portions of state grants and scholarships. Amounts received by students in the Company's schools under the FSEOG program in fiscal 2001 represented approximately 1% of the Company's net revenues.

Perkins. Eligible undergraduate students may borrow up to \$4,000 under the Perkins program during each academic year, with an aggregate maximum of \$20,000, at a 5% interest rate and with repayment delayed until nine months after a student ceases enrollment as at least a half-time student. Perkins loans are made available to those students who demonstrate the greatest financial need. Perkins loans are made from a revolving account, with 75% of new funding contributed by the U.S. Department of Education, and the remainder by the applicable school. Subsequent federal capital contributions, which must be matched by school funds, may be received if an institution meets certain requirements. Each school collects payments on Perkins loans from its former students and relends those funds to currently enrolled students. Collection and disbursement of Perkins loans is the responsibility of each participating institution. During fiscal 2001 the Company collected approximately \$3.5 million from its former students. In fiscal 2001, the Company's required matching contribution was approximately \$187,000. The Perkins loans disbursed to students in the Company's schools in fiscal 2001 represented approximately 1% of the Company's net revenues. Twelve of the Company's schools participate in the Perkins program.

Federal Work-Study. Under the FWS program, federal funds are made available to pay up to 75% of the cost of part-time employment of eligible students, based on their financial need, to perform work for the institution or for off-campus public or non-profit organizations. At least 7% of an institution's FWS allocation must be used to fund student employment in community service positions and at least one position must be in a literacy program or as a reading tutor. In fiscal 2001, FWS funds represented under 1% of the Company's net revenues.

Other Financial Assistance Sources

Students at several of the Company's schools participate in state grant programs. In fiscal 2001, approximately 3% of the Company's net revenues was derived from state grant programs. In addition, certain students at some of the Company's schools receive financial aid provided by the United States Department of Veterans Affairs, the United States Department of the Interior (Bureau of Indian Affairs) and the Rehabilitative Services Administration of the U.S. Department of Education (vocational rehabilitation funding). In fiscal 2001, financial assistance from such federal and state programs equaled approximately 1% of the Company's net revenues. The Art Institutes also provide institutional scholarships to qualified students. In fiscal 2001, institutional scholarships had a value equal to approximately 2.5% of the Company's net revenues. The Company has also arranged alternative supplemental loan programs that allow students to repay a portion of their loans after graduation and allow students with lower than average credit ratings to obtain loans. The primary objective of these loan programs is to lower the monthly payments required of students. Such loans are without recourse to the Company or its schools. In fiscal 2001, alternative loans represented approximately 5% of the Company's net revenue.

Availability of Lenders

During fiscal 2001, five lending institutions provided over 85% of all federally guaranteed loans to students attending the Company's schools. While the Company believes that other lenders would be willing to make federally guaranteed student loans to its students if loans were no longer available from its current lenders, there can be no assurances in this regard. In addition, the HEA requires the establishment of lenders of last resort in

every state to make certain loans to students at any school that cannot otherwise identify lenders willing to make federally guaranteed loans to its students.

One student loan guaranty agency (USA Group Guarantee Services, formerly United Student Aid Funds) currently guarantees approximately 95% of all federally guaranteed student loans made to students enrolled at the Company's schools. The Company believes that other guaranty agencies would be willing to guarantee loans to the Company's students if that agency ceased guaranteeing those loans or reduced the volume of those loans it guaranteed.

Federal Oversight of Title IV Programs

Each institution that participates in Title IV Programs must annually submit to the U.S. Department of Education an audit by an independent accounting firm of that school's compliance with Title IV Program requirements, as well as audited financial statements. The U.S. Department of Education also conducts compliance reviews, which include on-site evaluations, of several hundred institutions each year, and directs student loan guaranty agencies to conduct additional reviews relating to student loan programs. In addition, the Office of the Inspector General of the U.S. Department of Education conducts audits and investigations in certain circumstances. Under the HEA, accrediting agencies and state licensing agencies also have responsibilities for overseeing institutions' compliance with certain Title IV Program requirements. As a result, each participating institution is subject to frequent and detailed oversight and must comply with a complex framework of laws and regulations or risk being required to repay funds or becoming ineligible to participate in Title IV Programs.

Cohort Default Rates (CDR). Each institution that participates in the FFEL program must maintain a student loan CDR equal to or less than 25% (15% for the Perkins program) for three consecutive years or will no longer be eligible to participate in that program or the Federal Direct Student Loan Program for the remainder of the federal fiscal year in which the U.S. Department of Education determines that such institution has lost its eligibility and for the two subsequent federal fiscal years.

None of the Company's schools has had an FFEL cohort default rate of 25% or greater for any of the last three consecutive federal fiscal years. For federal fiscal year 1998, the most recent year for which such rates have been published, the average FFEL cohort default rate for borrowers at all proprietary institutions was 11.4%. For that year, the combined FFEL cohort default rate for all borrowers at the Company's schools was 9.9%. For federal fiscal year 1999, the combined preliminary FFEL cohort default rate for all borrowers at the Company's schools was 8.4% and its individual schools' preliminary rates ranged from 0% to 12.3%.

If an institution's FFEL cohort default rate equals or exceeds 25% in any of the three most recent federal fiscal years, or if its cohort default rate for loans under the Perkins program exceeds 15% for the most recent federal award year (i.e., July 1 through June 30), that institution may be placed on provisional certification status for up to four years. Provisional certification does not limit an institution's access to Title IV Program funds, but does subject that institution to closer review by the U.S. Department of Education and possible summary adverse action if that institution commits a material violation of Title IV Program requirements. To EDMC's knowledge, the U.S. Department of Education reviews an institution's compliance with the cohort default rate thresholds described in this paragraph only when that school is otherwise subject to a U.S. Department of Education certification review. Nine of the Company's schools had Perkins cohort default rates in excess of 15% for students who were to begin repayment during the federal award year ending June 30, 2000, the most recent year for which such rates have been calculated. For each of those schools, funds from the Perkins program equaled less than 5% of the school's net revenues in both fiscal 2000 and 2001. To date, only The Art Institute of Portland has been placed on provisional certification status for this reason, based upon the CDR for Perkins. If an institution is placed on such status for this reason and the institution reduces its Perkins cohort default rate to below 15% in a subsequent year, the institution can ask the U.S. Department of Education to remove the provisional status.

Each of the Company's schools maintains a student loan default management plan. Those plans provide for extensive loan counseling, methods to increase student persistence and completion rates and graduate employment rates, strategies to increase graduate salaries and, for most schools, the use of external agencies to assist the school with loan counseling and loan servicing if a student ceases to attend that school. Those activities are in addition to the loan servicing and collection activities of FFEL lenders and guaranty agencies.

Regulatory Oversight. The U.S. Department of Education is required to conduct periodic reviews of the eligibility and certification of every institution participating in Title IV Programs. A denial of recertification precludes a school from continuing to participate in Title IV Programs. All schools that submitted recertification applications during FY2001 received recertification.

During fiscal 2002, only The Art Institutes International at San Francisco is scheduled to apply for recertification.

The Art Institutes International at San Francisco, The Art Institute of California, The Art Institute of Las Vegas, Massachusetts Communications College, and The Art Institute of Charlotte are all provisionally certified by the United States Department of Education due to their recent acquisition by the Company. The Art Institute of Portland is provisionally certified due to its Perkins CDR being in excess of 30%. The U.S. Department of Education stated that when The Art Institute of Portland is below 30%, the Institute can request to be removed from the provisional status.

The HEA requires each accrediting agency recognized by the U.S. Department of Education to undergo comprehensive periodic review by the U.S. Department of Education to ascertain whether such accrediting agency is adhering to required standards. Many of the accrediting agencies that accredit the Company's schools will be reviewed by the U.S. Department of Education within the next two years. While EDMC knows of no reason that any of the accreditation agencies that its institutions use would not be approved, if an accreditation agency is not approved by the U.S. Department of Education, the institutions that are affected are given time to apply for accreditation from a different agency.

Financial Responsibility Standards. All institutions participating in Title IV Programs must satisfy a series of specific standards of financial responsibility. Institutions are evaluated for compliance with those requirements as part of the U.S. Department of Education's quadrennial recertification process and also annually as each institution submits its audited financial statements to the U.S. Department of Education. For the year ended June 30, 2001, the Company believes that, on an individual institution basis, each of its schools then participating in Title IV Programs satisfied the financial responsibility standards. The Illinois Institute of Art at Schaumburg, The Art Institute of Phoenix, The Art Institute of Los Angeles, The Art Institute of Los Angeles—Orange County and The Art Institute of Washington are combined with their main campuses, The Illinois Institute of Art at Chicago, The Art Institute of Colorado, The Art Institute of Pittsburgh, The Art Institute of Colorado and The Art Institute of Atlanta respectively, for that purpose.

Restrictions on Operating Additional Schools. The HEA generally requires that certain institutions, including proprietary schools, be in full operation for two years before applying to participate in Title IV Programs. However, under the HEA and applicable regulations, an institution that is certified to participate in Title IV Programs may establish an additional location and apply to participate in Title IV Programs at that location without reference to the two-year requirement if such additional location satisfies all other applicable requirements. In addition, a school that undergoes a change of ownership resulting in a change in control (as defined under the HEA) must be reviewed and recertified for participation in Title IV Programs under its new ownership. Most of a school's change of ownership application can be reviewed prior to the change of ownership. If the application is considered to be substantially complete, the U.S. Department of Education may generate a temporary Provisional Program Participation Agreement allowing the school's students to continue to receive

federal funding, subject to certain conditions. After the change of ownership and the remainder of the application is submitted, if the school is recertified, it is recertified on a provisional basis. During the time a school is provisionally certified, it may be subject to summary adverse action for a material violation of Title IV Program requirements and may not establish additional locations without prior approval from the U.S. Department of Education. However, provisional certification does not otherwise limit an institution's access to Title IV Program funds. The Company's expansion plans are based, in part, on its ability to add additional locations and acquire schools that can be recertified.

Certain of the state authorizing agencies and accrediting agencies with jurisdiction over the Company's schools also have requirements that may, in certain instances, limit the ability of the Company to open a new school, acquire an existing school or establish an additional location of an existing school. The Company does not believe that those standards will have a material adverse effect on the Company or its expansion plans.

The "90/10 Rule." Under a provision of the HEA commonly referred to as the "90/10 Rule," a proprietary institution such as each of EDMC's schools will cease to be eligible to participate in Title IV Programs if, on a cash accounting basis, more than 90% of its revenues for the prior fiscal year was derived from Title IV Programs. Any school that violates the 90/10 Rule immediately becomes ineligible to participate in Title IV Programs and is unable to apply to regain its eligibility until the following fiscal year. For those schools that disbursed federal financial aid during fiscal 2001, the percentage of revenues derived from Title IV Programs ranged from approximately 47% to 74%.

Restrictions on Payment of Bonuses, Commissions or Other Incentives. The HEA prohibits an institution from providing any commission, bonus or other incentive payment based directly or indirectly on success in securing enrollment or financial aid to any person or entity engaged in any student recruitment, admission or financial aid awarding activity. EDMC believes that its current compensation plans are in substantial compliance with HEA requirements.

State Authorization

Each of EDMC's schools is authorized to offer education programs and grant degrees or diplomas by the state in which such school is located. The level of regulatory oversight varies substantially from state to state. In some states, the schools are subject to licensure by the state education agency and also by a separate higher education agency. State laws establish standards for instruction, qualifications of faculty, location and nature of facilities, financial policies and responsibility and other operational matters. State laws and regulations may limit the ability of the Company to obtain authorization to operate in certain states or to award degrees or diplomas or offer new degree programs. Certain states prescribe standards of financial responsibility that are different from those prescribed by the U.S. Department of Education. The Company believes that each of its schools is in substantial compliance with applicable state authorizing and licensure laws.

Employees

As of June 30, 2001, EDMC employed 2,719 full-time and 989 part-time staff and faculty.

Competition

The postsecondary education market is highly competitive. The Art Institutes compete with traditional public and private two-year and four-year colleges and universities and other proprietary schools. Certain public and private colleges and universities may offer programs similar to those of The Art Institutes. Public institutions often receive government subsidies, government and foundation grants, tax-deductible contributions and other financial resources generally not available to proprietary schools. Accordingly, public institutions may have facilities and equipment superior to those in the private sector, and can offer lower tuition prices. However, tuition at private non-profit institutions is, on average, higher than The Art Institutes' tuition.

Seasonality in Results of Operations

EDMC has experienced seasonality in its results of operations primarily due to the pattern of student enrollment. Historically, EDMC's lowest quarterly revenues and income have been in the first quarter (July to September) of its fiscal year due to fewer students being enrolled during the summer months and the expenses incurred in preparation for the peak enrollment in the fall quarter (October to December). EDMC expects that this seasonal trend will continue.

ITEM 2—PROPERTIES

As of June 30, 2001, EDMC's schools were located in major metropolitan areas in 16 states. Typically, the schools occupy an entire building or several floors or portions of floors in a building. The Company and its subsidiaries currently lease the majority of their facilities.

The following table sets forth certain information as of June 30, 2001 with respect to the principal properties used by the Company and its subsidiaries:

Location (City/State)	Square Feet		Location (City/State)	Square Feet	
	Leased	Owned		Leased	Owned
Phoenix, AZ	58,635		Boston, MA	57,110	
Los Angeles, CA	56,150		Minneapolis, MN	67,750	
Orange County, CA	27,600		Las Vegas, NV	11,045	
San Diego, CA	20,885		New York, NY	42,245	
San Francisco, CA	26,965		Portland, OR	38,680	
Denver, CO	35,620	98,840	Philadelphia, PA(2)	158,810	
Ft. Lauderdale, FL(1)	122,850		Pittsburgh, PA	36,930	173,470
Atlanta, GA	117,895		Dallas, TX	95,420	
Charlotte, NC	16,915		Houston, TX	82,445	
Chicago, IL	62,657		Seattle, WA	58,975	74,635
Schaumburg, IL	42,300		Arlington, VA	32,330	

- (1) One of the properties occupied by The Art Institute of Fort Lauderdale is owned by a limited partnership that includes among its limited partners one current member of EDMC's management who is also a director.
- (2) One of the properties occupied by The Art Institute of Philadelphia is owned indirectly by a limited partnership that includes among its limited partners one current member of EDMC's management who is also a director as well as one other current director of EDMC.

ITEM 3—LEGAL PROCEEDINGS

The Company is a defendant in certain legal proceedings arising out of the conduct of its business. In the opinion of management, based upon its investigation of these claims and discussion with legal counsel, the ultimate outcome of such legal proceedings, individually and in the aggregate, will not have a material adverse effect on the consolidated financial position, results of operations or liquidity of the Company.

ITEM 4—SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Not applicable.

PART II

ITEM 5—MARKET FOR THE REGISTRANT’S COMMON EQUITY AND RELATED SHAREHOLDER MATTERS

The Common Stock is traded on the Nasdaq National Market System under the symbol “EDMC.” As of September 11, 2001, there were 30,351,322 shares of Common Stock outstanding held by 463 holders of record. The prices set forth below reflect the high and low sales prices for the Company’s Common Stock, as reported in the consolidated transaction reporting system of the Nasdaq National Market System.

<u>Three Months Ended</u>	<u>2000</u>		<u>2001</u>	
	<u>High</u>	<u>Low</u>	<u>High</u>	<u>Low</u>
September 30	\$21.13	\$12.38	\$26.94	\$17.75
December 31	14.81	8.69	38.38	24.75
March 31	14.63	11.00	37.81	26.06
June 30	18.69	14.88	40.05	28.92

EDMC has not declared or paid any cash dividends on its capital stock during the past two years. EDMC currently intends to retain future earnings, if any, to fund the development and growth of its business and does not anticipate paying any cash dividends in the foreseeable future.

ITEM 6—SELECTED FINANCIAL DATA

The following summary consolidated financial and other data should be read in conjunction with the Company's Consolidated Financial Statements and Notes thereto filed in response to Item 8 and the information included in response to Item 7 below. Most of the summary data presented below is derived from the Company's consolidated financial statements audited by Arthur Andersen LLP, independent public accountants, whose report covering the financial statements as of June 30, 2000 and 2001 and for each of the three years in the period ended June 30, 2001 also is filed in response to Item 8 below. The summary consolidated income statement data for the years ended June 30, 1997 and 1998 and the summary consolidated balance sheet data as of June 30, 1997, 1998 and 1999 are derived from audited financial statements not included herein.

	Year ended June 30,				
	1997	1998	1999	2000	2001
	(Dollars in thousands, except per share amounts)				
Income Statement Data:					
Net revenues	\$182,849	\$221,732	\$260,805	\$307,249	\$370,681
Net income	9,985	14,322	18,752	22,530	28,978
Dividends on Series A Preferred Stock(1)	83	—	—	—	—
Other Series A Preferred Stock Transactions(1)	403	—	—	—	—
Per Share Data(1):					
Basic:					
Net income	\$.40	\$.50	\$.64	\$.78	\$.97
Weighted average number of shares outstanding, in thousands(2)	23,878	28,908	29,314	28,964	29,742
Diluted:					
Net income	\$.36	\$.48	\$.61	\$.75	\$.93
Weighted average number of shares outstanding, in thousands(2)	27,342	29,852	30,615	29,921	31,016
Other Data:					
Capital expenditures(3)	\$ 18,942	\$ 18,814	\$ 55,892	\$ 58,149	\$ 38,822
Enrollment at beginning of fall quarter(4)	15,838	18,763	21,518	24,502	27,999
	As of June 30,				
	1997	1998	1999	2000	2001
	(in thousands)				
Balance Sheet Data:					
Cash and cash equivalents	\$ 33,227	\$ 47,310	\$ 32,871	\$ 39,538	\$ 47,290
Receivables, net	10,547	10,292	12,490	14,931	18,945
Current assets	48,886	65,623	55,709	66,713	81,816
Total assets	126,292	148,783	178,746	240,675	283,946
Current liabilities	36,178	38,097	45,188	62,891	70,303
Long-term debt (including current portion)	34,031	38,382	37,231	64,283	53,660
Shareholders' investment	57,756	73,325	96,805	112,950	159,949

- (1) Dividends on the outstanding shares of Series A Preferred Stock, dividends accrued but not paid on outstanding shares of Series A Preferred Stock and a redemption premium paid upon redemption of 75,000 shares of Series A Preferred Stock have been deducted from net income in calculating earnings per share.
- (2) The weighted average shares outstanding used to calculate basic income per share does not include potentially dilutive securities (such as stock options, warrants and convertible preferred stock). Diluted income per share includes, where dilutive, the equivalent shares of Common Stock calculated under the treasury stock method for the assumed exercise of options and warrants and conversion of shares of Series A Preferred Stock.
- (3) Capital expenditures for fiscal 1999, 2000 and 2001 reflect approximately \$5.1 million, \$13.2 million and \$4.5 million included in accounts payable at year-end, respectively.
- (4) Excludes students enrolled in programs at those colleges and universities with which the Company has consulting arrangements.

ITEM 7—MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion of the Company’s results of operations and financial condition should be read in conjunction with the information filed in response to Item 6 above and Item 8 below. Unless otherwise specified, any reference to a “year” is to a fiscal year ended June 30.

Background

EDMC is among the largest providers of proprietary postsecondary education in the United States, based on student enrollment and revenues. Through its main operating unit, The Art Institutes, the Company offers bachelor’s and associate’s degree programs and non-degree programs in the areas of design, media arts, culinary arts and fashion. The Company has provided career-oriented education programs for over 35 years, and its Art Institutes have more than 125,000 graduates. As of June 30, 2001, the Company operated 24 schools in 20 major metropolitan areas throughout the United States.

Net revenues, income before interest and taxes and net income increased in each of the last two years. Net revenues are presented after deducting refunds, scholarships and other adjustments. Net revenues increased 42.1% to \$370.7 million in 2001 from \$260.8 million in 1999. Income before interest and taxes increased 56.7% to \$49.7 million in 2001 from \$31.7 million in 1999. Net income increased by 54.5% to \$29.0 million in 2001 from \$18.8 million in 1999. Average quarterly student enrollment at the Company’s schools was 25,549 in 2001 compared to 19,325 in 1999. The increase in average enrollment relates to, among other factors, new education programs and additional school locations, along with expanded bachelor’s degree and evening degree program offerings.

The Company’s revenues consist of tuition and fees, student housing fees and student supply store and restaurant sales. In 2001, the Company derived 89.8% of its net revenues from net tuition and fees paid by, or on behalf of, its students. Tuition revenue generally varies based on the average tuition charge per credit hour and the average student population. Student supply store and housing revenue is largely a function of the average student population. The average student population is influenced by the number of continuing students attending school at the beginning of a fiscal period and by the number of new students entering school during such period. New students enter The Art Institutes at the beginning of each academic quarter, which typically commence in January, April, July and October. The Company believes that the size of its student population is influenced by the number of graduating high school students, the attractiveness of its program offerings, the effectiveness of its marketing efforts, changes in technology, the persistence of its students, the length of its education programs and general economic conditions. The introduction of additional program offerings at existing schools and the establishment of new schools (through acquisition or start-up) are important factors influencing the Company’s average student population.

Tuition increases have been implemented in varying amounts in each of the past several years. Historically, the Company has been able to pass along cost increases through increases in tuition. The Company believes that it can continue to increase tuition as educational costs at other postsecondary institutions, both public and private, continue to rise. The Company’s schools implemented tuition rate increases averaging approximately 7% during 2001. Tuition rates vary by geographic region, but are generally consistent by program at the respective schools.

The majority of students at The Art Institutes rely on funds received under various government-sponsored student financial aid programs, especially Title IV Programs, to pay a substantial portion of their tuition and other education-related expenses. For the year ended June 30, 2001, approximately 60% of the Company’s net revenues were indirectly derived from Title IV Programs.

Educational services expense consists primarily of costs related to the development, delivery and administration of the Company’s education programs. Major cost components are faculty compensation, administrative salaries, costs of educational materials, facility and school occupancy costs, information systems

costs, bad debt expense and depreciation and amortization of property and equipment. The Company's faculty comprised approximately 46% full-time and 54% part-time employees for 2000 and approximately 49% full-time and 51% part-time employees for 2001.

General and administrative expense consists of marketing and student admissions expenses and certain central staff departmental costs such as executive management, finance and accounting, legal and corporate development and other departments that do not provide direct services to the Company's students. The Company has centralized many of these services to gain consistency in management reporting, efficiency in administrative effort and control of costs.

Amortization of intangibles relates to the values assigned to identifiable intangible assets and goodwill. These intangible assets arose principally from the acquisitions of the schools discussed below.

In October 1998, the Company acquired the assets of Socrates Distance Learning Technologies Group for approximately \$0.5 million in cash. This acquisition was made to further the development of the Company's distance learning capabilities.

In August 1999, the Company acquired the outstanding stock of the American Business & Fashion Institute in Charlotte, North Carolina, for \$0.5 million in cash. The school was renamed The Art Institute of Charlotte.

In August 1999, the Company acquired the outstanding stock of Massachusetts Communications College in Boston, Massachusetts for approximately \$7.2 million in cash. Subsequent to June 30, 2001, the school was renamed The New England Institute of Art and Communications.

In October 2000, the Company acquired the outstanding stock of The Art Institute of California located in San Diego, California for approximately \$9.8 million in cash.

In April 2001, the Company acquired the outstanding stock of the Design Institute located in Las Vegas, Nevada for approximately \$2.1 million in cash. The school was renamed The Art Institute of Las Vegas.

Start-up schools and smaller acquisitions are expected to incur operating losses during the first two to three years following their opening or purchase. The combined operating losses of the Company's newer schools were approximately \$6.7 million and \$9.6 million in fiscal 2000 and 2001, respectively.

Results of Operations

The following table sets forth for the periods indicated the percentage relationships of certain income statement items to net revenues.

	Year ended June 30,		
	1999	2000	2001
Net revenues	100.0%	100.0%	100.0%
Costs and expenses:			
Educational services	65.5	65.5	65.4
General and administrative	21.9	21.5	20.7
Amortization of intangibles	0.5	0.5	0.5
	<u>87.8</u>	<u>87.5</u>	<u>86.6</u>
Income before interest and taxes	12.2	12.5	13.4
Interest expense, net	—	0.3	0.6
Income before income taxes	12.2	12.2	12.8
Provision for income taxes	5.0	4.9	5.0
Net income	<u>7.2%</u>	<u>7.3%</u>	<u>7.8%</u>

Year Ended June 30, 2001 Compared with Year Ended June 30, 2000

Net Revenues

Net revenues increased by 20.6% to \$370.7 million in 2001 from \$307.2 million in 2000. The revenue increase was primarily due to an increase in average quarterly student enrollment (\$33.4 million) and tuition increases of approximately 7.0% (\$24.2 million). The average academic year (three academic quarters) tuition rate for a student attending classes at an Art Institute on a recommended full schedule increased to \$12,584 in 2001 from \$11,703 in 2000.

Net housing revenues increased by 20.8% to \$21.9 million in 2001 from \$18.1 million in 2000 and revenues from the sale of educational materials in 2001 increased by 15.1% to \$15.8 million. Both increased primarily as a result of higher average student enrollment. Refunds increased to \$8.9 million in 2001 from \$8.6 million in 2000. As a percentage of gross revenue, refunds decreased from 2000.

Educational Services

Educational services expense increased by \$41.1 million, or 20.4%, to \$242.3 million in 2001 from \$201.2 million in 2000. The increase was primarily due to additional costs required to service higher student enrollment, accompanied by normal cost increases for wages and other services at the schools owned by EDMC prior to 2000 (\$26.9 million) and schools added in 2000 and 2001 (\$14.9 million). Higher costs associated with establishing and supporting new schools and developing new education programs contributed to the increase. As a percentage of net revenues, educational services expense decreased slightly between years.

General and Administrative

General and administrative expense increased by 15.9% to \$76.7 million in 2001 from \$66.2 million in 2000 due to the incremental marketing and student admissions expenses incurred to generate higher student enrollment at the schools owned by EDMC prior to 2000 (\$2.2 million) and additional marketing and student admissions expenses at the schools added in 2000 and 2001 (\$4.6 million). General and administrative expense decreased approximately 80 basis points as a percentage of net revenues in 2001 compared to 2000, reflecting operating leverage at the schools operated by EDMC for more than two years.

Amortization of Intangibles

Amortization of intangibles increased by \$0.5 million, or 30.8%, to \$2.0 million in 2001 from \$1.5 million in 2000, as a result of additional amortization associated with fiscal 2001 acquisitions and on-line curriculum. Goodwill amortization was approximately \$1.0 million for fiscal 2001.

Interest Expense, Net

The Company had net interest expense of \$2.3 million in 2001 as compared to \$726,000 in 2000. This change is attributable to increased average borrowings related primarily to capital expenditures and acquisitions, offset by a lower effective interest rate. The average outstanding debt balance was approximately \$28.2 million in 2001, up from \$15.6 million in 2000. Additionally, interest incurred in connection with construction of facilities in Denver and Pittsburgh was capitalized during the respective construction periods in 2000.

Provision for Income Taxes

The Company's effective tax rate decreased to 38.9% in 2001 from 40.1% in 2000. This reduction primarily reflects a more favorable distribution of taxable income among the states in which the Company operates and a decrease in nondeductible expenses as a percentage of taxable income. The effective rates differed from the combined federal and state statutory rates due to expenses that are nondeductible for income tax purposes.

Net Income

Net income increased by \$6.5 million or 28.6% to \$29.0 million in 2001 from \$22.5 million in 2000. The increase resulted from improved operations at the Company's schools owned prior to 2000 and a lower effective income tax rate, offset by increased amortization of intangible and interest expense.

Year Ended June 30, 2000 Compared with Year Ended June 30, 1999

Net Revenues

Net revenues increased by 17.8% to \$307.2 million in 2000 from \$260.8 million in 1999. The revenue increase was primarily due to an increase in average quarterly student enrollment (\$25.4 million) and tuition increases of approximately 5% (\$16.2 million). The average academic year (three academic quarters) tuition rate for a student attending classes at an Art Institute on a recommended full schedule increased to \$11,703 in 2000 from \$11,262 in 1999.

Net housing revenues increased by 23.2% to \$18.1 million in 2000 from \$14.7 million in 1999 and revenues from the sale of educational materials in 2000 increased by 11.8% to \$13.8 million. Both increased primarily as a result of higher average student enrollment. Refunds increased from \$8.0 million in 1999 to \$8.6 million in 2000. As a percentage of gross revenue, refunds decreased from 1999.

Educational Services

Educational services expense increased by \$30.4 million, or 17.8%, to \$201.2 million in 2000 from \$170.7 million in 1999. The increase was primarily due to additional costs required to service higher student enrollment, accompanied by normal cost increases for wages and other services at the schools owned by EDMC prior to 1999 (\$23.0 million) and schools added in 1999 and 2000 (\$7.5 million). Higher costs associated with establishing and supporting new schools and developing new education programs contributed to the increase. As a percentage of net revenues, educational services expense was consistent between years at 65.5%. This represents an improvement over the 66.4% of net revenues in the prior year, primarily a result of margin improvements in various expenses, such as rent, bad debt, and other operating costs.

General and Administrative

General and administrative expense increased by 15.8% to \$66.2 million in 2000 from \$57.2 million in 1999 due to the incremental marketing and student admissions expenses incurred to generate higher student enrollment at the schools owned by EDMC prior to 1999 (\$5.0 million), and additional marketing and student admissions expenses at the schools added in 1999 and 2000 (\$3.1 million). General and administrative expense increased slightly as a percentage of net revenues in 2000 compared to 1999 as a result of increased advertising expenditures designed to promote awareness of and generate inquiries about the newer locations and new program offerings.

Amortization of Intangibles

Amortization of intangibles increased by \$0.3 million, or 25.6%, to \$1.5 million in 2000 from \$1.2 million in 1999, as a result of additional amortization associated with the fiscal 2000 additions.

Interest Expense (Income), Net

The Company had net interest expense of \$726,000 in 2000 as compared to interest income of \$113,000 in 1999. The average outstanding debt balance increased from \$4.6 million in 1999 to \$15.6 million in 2000. Accordingly, more interest cost on borrowings has been offset against interest earned on investments.

Provision for Income Taxes

The Company's effective tax rate decreased to 40.1% in 2000 from 41.1% in 1999. This reduction reflects a more favorable distribution of taxable income among the states in which the Company operates and a decrease

in non-deductible expenses as a percentage of taxable income. The effective rates differed from the combined federal and state statutory rates due to expenses that are nondeductible for income tax purposes.

Net Income

Net income increased by \$3.8 million or 20.1% to \$22.5 million in 2000 from \$18.8 million in 1999. The increase resulted from improved operations at the Company's schools owned prior to 1999 and a lower effective income tax rate.

Seasonality and Other Factors Affecting Quarterly Results

The Company's quarterly revenues and income fluctuate primarily as a result of the pattern of student enrollment. The Company experiences a seasonal increase in new enrollment in the fall (fiscal year second quarter), which is traditionally when the largest number of new high school graduates begin postsecondary education. Some students choose not to attend classes during summer months, although the Company's schools encourage year-round attendance. As a result, total student enrollment at the Company's schools is highest in the fall quarter and lowest in the summer months (fiscal year first quarter). The Company's costs and expenses, however, do not fluctuate as significantly as revenues on a quarterly basis. The Company anticipates that the seasonal pattern in revenues and earnings will continue in the future.

Quarterly Financial Results (unaudited)

The following table sets forth the Company's quarterly results for 2000 and 2001.

	<u>Sept. 30</u> <u>(Summer)</u>	<u>Dec. 31</u> <u>(Fall)</u>	<u>Mar. 31</u> <u>(Winter)</u>	<u>June 30</u> <u>(Spring)</u>
	(dollars in thousands, except per share data)			
<u>2000</u>				
Net revenues	\$60,850	\$ 87,023	\$ 83,195	\$76,181
Income before interest and taxes	\$ 1,693	\$ 19,566	\$ 11,968	\$ 5,115
Income before income taxes	\$ 1,570	\$ 19,247	\$ 11,881	\$ 4,918
Net income	\$ 926	\$ 11,524	\$ 7,113	\$ 2,967
Earnings per share				
—Basic	\$.03	\$.40	\$.25	\$.10
—Diluted	\$.03	\$.39	\$.24	\$.10
<u>2001</u>				
Net revenues	\$72,561	\$103,112	\$100,366	\$94,642
Income before interest and taxes	\$ 2,511	\$ 24,639	\$ 16,009	\$ 6,516
Income before income taxes	\$ 1,896	\$ 23,816	\$ 15,570	\$ 6,118
Net income	\$ 1,156	\$ 14,531	\$ 9,498	\$ 3,793
Earnings per share				
—Basic	\$.04	\$.49	\$.32	\$.13
—Diluted	\$.04	\$.47	\$.30	\$.12

Earnings per share amounts for each quarter are required to be calculated independently and, therefore, may not equal the amount calculated for the year.

Liquidity and Capital Resources

The Company's cash flow from operations has been the primary source of financing for capital expenditures and growth. Additionally, the Company maintains a revolving credit facility. Cash flow from operations was \$36.4 million, \$47.7 million, and \$70.9 million for 1999, 2000, and 2001, respectively. Cash flow from operating and investing activities does not reflect capital expenditures of approximately \$5.1 million, \$13.2 million, and \$4.5 million which are included in accounts payable as of June 30, 1999, 2000 and 2001, respectively.

Additionally, cash flows from operating and financing activities does not reflect income tax deductions related to the exercise of options of \$2.7 million, \$0.9 million and \$9.8 million. These deductions do not effect the Company's tax provision; the benefit is recorded as additional paid-in capital in the accompanying consolidated balance sheets. Therefore, the change in the applicable balance sheet accounts (accounts payable, property and equipment, accrued liabilities and additional paid in capital) does not directly correlate to the corresponding amounts in the accompanying statement of cash flows.

The Company had net working capital of \$11.5 million as of June 30, 2001, up from \$3.8 million as of June 30, 2000. This change is due primarily to the timing of payments made for capital expenditures. As noted above, purchases of property and equipment included in accounts payable decreased approximately \$8.7 million from June 30, 2000 to June 30, 2001. Advanced payments increased approximately \$8.1 million and \$14.9 million as compared to the respective prior year-end balances at June 30, 2000 and 2001. Increases in enrollment, tuition and monies received in connection with alternative loan programs offered to students, as well as arrangements offering incentives for early tuition payments have all contributed to this increase. Unearned revenue of approximately \$446,000 and \$1.7 million was included with advanced payments as of June 30, 2000 and 2001, respectively.

As of June 30, 2001, gross trade accounts receivable increased by \$7.3 million, or 27.9%, to \$33.4 million from the prior year primarily due to the higher enrollment and tuition rates. Additionally, certain recently acquired schools have not yet been converted to the quarter system used by most of The Art Institutes and were in session as of year-end. Under the payment terms, these balances would be reduced by the end of the applicable class sessions. Although tuition increases have exceeded corresponding increases in federal financial aid sources, the Company has arranged for alternative financing sources to manage its credit risk. The allowance for doubtful accounts was \$9.4 million, \$14.1 million, and \$17.4 million as of June 30, 1999, 2000, and 2001, respectively. This represents increases of 12.6%, 50.4%, and 23.6% in the allowance for doubtful accounts for 1999, 2000, and 2001, respectively. The Company determines its reserve for accounts receivable by categorizing gross receivables based upon the enrollment status of the student (in-school, out of school, summer leave of absence, and collections) then establishing a reserve based on the likelihood of collections (in-school receivables being the lowest percent reserved). The Company provides for extended payment terms beyond graduation (generally six months). As more students have utilized this option, the out-of-school category has increased as a percentage of gross receivables which has resulted in an increase in the corresponding allowance against these balances. Therefore, the change between years in the allowance results from both the overall increase in trade receivables as well as changes in the distribution of gross receivables among the categories.

The Credit Agreement (the "Credit Agreement"), which the Company entered into during fiscal 2000, currently allows for maximum borrowings of \$100.0 million through its expiration on February 18, 2005. Borrowings under this facility are unsecured and bear interest at one of three rates set forth in the Credit Agreement, at the election of the Company. Certain outstanding letters of credit reduce this facility. As of June 30, 2001, the Company had approximately \$45.4 million of borrowing capacity available under the Credit Agreement. As of June 30, 2001, the Company was in compliance with all covenants under the Credit Agreement. As of June 30, 2001, the average interest rate for borrowings under the Credit Agreement was 4.5%.

Borrowings under the Credit Agreement are used by the Company primarily to fund working capital needs resulting from the seasonal pattern of cash receipts throughout the year. The level of accounts receivable reaches a peak immediately after the billing of tuition and fees at the beginning of each academic quarter. Collection of these receivables is heaviest at the start of each academic quarter.

Subsequent to year-end, the Company and its lenders amended and restated the Credit Agreement to increase allowable borrowings from \$100 million to \$200 million. The Amended and Restated Credit Agreement, which will expire September 20, 2004, is secured by certain assets of the Company and provides the Company the ability to borrow up to \$150 million on a revolving basis and \$50 million in the form of a term loan (collectively, the "Secured Credit Facilities"). The Secured Credit Facilities contain the customary covenants that, among other matters, require the Company to meet specified financial ratios, restrict the repurchase of Common Stock and limit the incurrence of additional indebtedness.

Capital Expenditures

Capital expenditures made during the three years ended June 30, 2001 reflect the implementation of the Company's initiatives emphasizing the addition of new schools and education programs and investment in classroom technology. The Company's capital expenditures (on an accrual basis) were \$55.9 million, \$58.1 million, and \$38.8 million, for 1999, 2000, and 2001, respectively. The Company expects that total capital spending for 2002 will remain relatively consistent as a percentage of net revenues, as compared to 2001. The Company anticipates that these expenditures will be financed primarily through cash flow from operations and supplemented as needed with borrowings under the revolving credit facility. The anticipated expenditures relate principally to the investment in schools acquired or started during the previous several years and to be added in 2002, continued improvements to current facilities, additional or replacement school and housing facilities and classroom and administrative technology.

The Company leases the majority of its facilities. Future commitments on existing leases will be paid from cash provided by operating activities.

Regulations

The Company indirectly derived approximately 60% of its net revenues from Title IV Programs in 2001. U.S. Department of Education regulations prescribe the timing of disbursements of funds under Title IV Programs. Students must apply for a new loan for each academic year. Lenders generally provide loan funds in multiple disbursements each academic year. For first-time students in their first academic quarter, the initial loan disbursement is generally received at least 30 days after the commencement of that academic quarter. Otherwise, the first loan disbursement is received, at the earliest, 10 days before the commencement of the student's academic quarter.

U.S. Department of Education regulations require Title IV Program funds received by the Company's schools in excess of the tuition and fees owed by the relevant students at that time to be, with these students' permission, maintained and classified as restricted until they are billed for the portion of their education program related to those funds. Funds transferred through electronic funds transfer programs are held in a separate cash account and released when certain conditions are satisfied. These restrictions have not significantly affected the Company's ability to fund daily operations.

Education institutions participating in Title IV Programs must satisfy a series of specific standards of financial responsibility. The U.S. Department of Education has adopted standards to determine an institution's financial responsibility to participate in Title IV Programs. The regulations establish three ratios: (i) the equity ratio, intended to measure an institution's capital resources, ability to borrow and financial viability; (ii) the primary reserve ratio, intended to measure an institution's ability to support current operations from expendable resources; and (iii) the net income ratio, intended to measure an institution's profitability. Each ratio is calculated separately, based on the figures in the institution's most recent annual audited financial statements, and then weighted and combined to arrive at a single composite score. Such composite score must be at least 1.5 for the institution to be deemed financially responsible without conditions or additional oversight.

Regulations promulgated under the HEA also require all proprietary education institutions to comply with the "90/10 Rule," which prohibits participating schools from deriving 90% or more of total revenue from Title IV Programs in any year.

If an institution fails to meet any of these requirements, it may be deemed to be not financially responsible by the U.S. Department of Education, or otherwise ineligible to participate in Title IV Programs. The Company believes that all of its participating schools met these requirements as of June 30, 2001.

Effect of Inflation

The Company does not believe its operations have been materially affected by inflation.

Impact of New Accounting Standards

In June 2001, SFAS No. 141, “Business Combinations” was issued. The statement addresses financial accounting and reporting for business combinations and supersedes APB Opinion No. 16, “Business Combinations,” and FASB statement No. 38 “Accounting for Preacquisition Contingencies of Purchased Enterprises.” The statement requires that all business combinations initiated after June 30, 2001 be accounted for using the purchase method. SFAS 141 is effective July 1, 2001. The Company’s adoption of SFAS 141 will not have a material impact on the Company’s financial position or results of operations.

In June 2001, SFAS No. 142 “Goodwill and Other Intangible Assets” was issued. This Statement addresses financial accounting and reporting for acquired goodwill and other intangible assets and supersedes APB Opinion No. 17, “Intangible Assets”. It addresses how intangible assets that are acquired individually or with a group of other assets (but not those acquired in a business combination) should be accounted for in financial statements upon their acquisition. This Statement also addresses how goodwill and other intangible assets should be accounted for after they have been initially recognized in the financial statements. The Company has adopted this standard as of July 1, 2001. The Company is required to complete a transitional goodwill impairment test for all goodwill at the reporting unit level by December 31, 2001 and is currently preparing for this. Adopting SFAS 142 will affect the financial position and results of operations because goodwill will no longer be amortized. It is anticipated that the adoption of this standard in fiscal 2002 will decrease amortization of intangibles expense by approximately \$1 million, reduce the effective tax rate (but not the tax provision) by less than 1%, and increase diluted earnings per share by approximately \$.03 for the fiscal year.

Risk Factors

In addition to the important factors described elsewhere in this Annual Report on Form 10-K, the following factors, among others, could affect the Company’s business, results of operations, financial condition and prospects in fiscal 2002 and later years: (i) the perceptions of the U.S. Congress, the U.S. Department of Education and the public concerning proprietary postsecondary education institutions to the extent those perceptions could result in changes in the HEA in connection with its reauthorization; (ii) EDMC’s ability to comply with federal and state regulations and accreditation standards, including any changes therein or changes in the interpretation thereof; (iii) the continued availability of alternative loan programs to students at the Company’s schools; (iv) the Company’s ability to foresee changes in the skills required of its graduates and to design new courses and programs to develop those skills in a cost effective and timely manner; (v) the ability of the Company to gauge successfully which markets are underserved in the skills that the Company’s schools teach; (vi) the Company’s ability to continue to attract and retain students by maintaining the appropriate capacity and system operations; (vii) security risks that the Company’s computer networks may be vulnerable to which could disrupt operations and require the Company to expend significant resources; (viii) the Company’s ability to gauge appropriate acquisition and start-up opportunities and to manage and integrate them successfully, as well as obtain necessary regulatory approvals for the acquisitions; (ix) the Company’s ability to defend litigation successfully; (x) proprietary rights and intellectual property that the Company relies upon may not be adequately protected by law; (xi) the Company’s ability to recruit and retain key personnel; (xii) anti-takeover provisions in the Company’s charter documents could disincent a takeover of the Company or serve as a disincentive; (xiii) competitive pressures from other education institutions; and (xiv) general economic conditions, including stock market volatility and uncertainty arising from the terrorist attacks of September 11, 2001.

ITEM 7A—QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS

The fair values and carrying amounts of the Company’s financial instruments, primarily accounts receivable and debt, are approximately equivalent. The debt instruments bear interest at floating rates based upon market rates or at fixed rates that approximate market rates. All other financial instruments are classified as current and will be utilized within the next operating cycle.

ITEM 8—FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Shareholders of Education Management Corporation and Subsidiaries:

We have audited the accompanying consolidated balance sheets of Education Management Corporation (a Pennsylvania corporation) and Subsidiaries as of June 30, 2000 and 2001, and the related consolidated statements of income, shareholders' investment and cash flows for each of the three years in the period ended June 30, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Education Management Corporation and Subsidiaries as of June 30, 2000 and 2001, and their results of operations and their cash flows for each of the three years in the period ended June 30, 2001 in conformity with accounting principles generally accepted in the United States.

s/ Arthur Andersen LLP

Pittsburgh, Pennsylvania,
July 27, 2001

EDUCATION MANAGEMENT CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except share data)

	As of June 30,	
	2000	2001
Assets		
Current assets:		
Cash and cash equivalents, including restricted balances of \$679 and \$218	\$ 39,538	\$ 47,290
Receivables:		
Trade, net of allowances of \$14,088 and \$17,410	12,057	16,032
Notes, advances and other	2,874	2,913
Inventories	3,145	3,528
Deferred and prepaid income taxes	4,676	7,350
Other current assets	4,423	4,703
Total current assets	66,713	81,816
Property and equipment, net	134,738	149,482
Deferred income taxes and other long-term assets	9,156	9,590
Intangible assets, net of amortization of \$6,065 and \$8,042	30,068	43,058
Total assets	\$240,675	\$283,946
Liabilities and shareholders' investment		
Current liabilities:		
Current portion of long-term debt	\$ 16	\$ 26
Accounts payable	19,898	10,795
Accrued liabilities	13,062	14,692
Advance payments	29,915	44,790
Total current liabilities	62,891	70,303
Long-term debt, less current portion	64,267	53,634
Other long-term liabilities	567	60
Commitments and contingencies		
Shareholders' investment:		
Common Stock, par value \$.01 per share; 60,000,000 shares authorized; 29,877,025 and 30,479,880 shares issued	299	305
Additional paid-in capital	96,585	108,463
Treasury stock, 907,446 and 216,945 shares at cost	(9,733)	(3,596)
Retained earnings	25,799	54,777
Total shareholders' investment	112,950	159,949
Total liabilities and shareholders' investment	\$240,675	\$283,946

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

EDUCATION MANAGEMENT CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(Dollars in thousands, except per share amounts)

	<u>For the years ended June 30,</u>		
	<u>1999</u>	<u>2000</u>	<u>2001</u>
Net revenues	\$260,805	\$307,249	\$370,681
Costs and expenses:			
Educational services	170,742	201,187	242,313
General and administrative	57,162	66,209	76,716
Amortization of intangibles	1,203	1,511	1,977
	<u>229,107</u>	<u>268,907</u>	<u>321,006</u>
Income before interest and taxes	31,698	38,342	49,675
Interest expense (income), net	(113)	726	2,275
Income before income taxes	31,811	37,616	47,400
Provision for income taxes	13,059	15,086	18,422
Net income	<u>\$ 18,752</u>	<u>\$ 22,530</u>	<u>\$ 28,978</u>
Earnings per share:			
Basic	\$.64	\$.78	\$.97
Diluted	\$.61	\$.75	\$.93
Weighted average number of shares outstanding (in 000's):			
Basic	29,314	28,964	29,742
Diluted	30,615	29,921	31,016

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

EDUCATION MANAGEMENT CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)

	For the years ended June 30,		
	1999	2000	2001
Cash flows from operating activities:			
Net income	\$18,752	\$22,530	\$28,978
Adjustments to reconcile net income to net cash flows from operating activities:			
Depreciation and amortization	17,440	21,043	26,055
Deferred credit for income taxes	(1,992)	(1,895)	(2,728)
Changes in current assets and liabilities:			
Receivables	(3,655)	(1,237)	(3,263)
Inventories	(105)	(978)	(383)
Other current assets	(650)	(1,312)	(1,458)
Accounts payable	57	(724)	(1,161)
Accrued liabilities	3,940	2,148	11,567
Advance payments	2,571	8,090	13,318
Total adjustments	17,606	25,135	41,947
Net cash flows from operating activities	36,358	47,665	70,925
Cash flows from investing activities:			
Acquisition of subsidiaries, net of cash acquired	(500)	(8,602)	(12,065)
Expenditures for property and equipment	(50,821)	(50,059)	(47,477)
Other items, net	(389)	(1,008)	(1,150)
Net cash flows from investing activities	(51,710)	(59,669)	(60,692)
Cash flows from financing activities:			
Net activity under revolving credit facilities	1,500	27,650	(10,625)
Principal payments on debt	(2,651)	(1,666)	(102)
Net proceeds from issuance of Common Stock	2,205	1,925	8,246
Repurchase of shares	(141)	(9,238)	—
Net cash flows from financing activities	913	18,671	(2,481)
Net change in cash and cash equivalents	(14,439)	6,667	7,752
Cash and cash equivalents, beginning of year	47,310	32,871	39,538
Cash and cash equivalents, end of year	\$32,871	\$39,538	\$47,290

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

EDUCATION MANAGEMENT CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' INVESTMENT
(Dollars in thousands)

	<u>Common Stock at Par Value</u>	<u>Additional Paid-in Capital</u>	<u>Treasury Stock</u>	<u>Stock Subscriptions Receivable</u>	<u>Retained Earnings</u>	<u>Total Shareholders' Investment</u>
Balance, June 30, 1998	\$ 290	\$ 88,880	\$ (354)	\$ (8)	\$(15,483)	\$ 73,325
Net income	—	—	—	—	18,752	18,752
Payments received on stock subscriptions receivable	—	—	—	8	—	8
Purchase of Common Stock	—	—	(141)	—	—	(141)
Exercise of stock options	5	4,278	—	—	—	4,283
Issuance of Common Stock under employee stock purchase plan	—	578	—	—	—	578
Balance, June 30, 1999	<u>295</u>	<u>93,736</u>	<u>(495)</u>	<u>—</u>	<u>3,269</u>	<u>96,805</u>
Net income	—	—	—	—	22,530	22,530
Purchase of Common Stock	—	—	(9,238)	—	—	(9,238)
Exercise of stock options	3	2,126	—	—	—	2,129
Issuance of Common Stock under employee stock purchase plan	1	723	—	—	—	724
Balance, June 30, 2000	<u>299</u>	<u>96,585</u>	<u>(9,733)</u>	<u>—</u>	<u>25,799</u>	<u>112,950</u>
Net income	—	—	—	—	28,978	28,978
Exercise of stock options	6	11,265	6,017	—	—	17,288
Issuance of Common Stock under employee stock purchase plan	—	613	120	—	—	733
Balance, June 30, 2001	<u>\$ 305</u>	<u>\$108,463</u>	<u>\$(3,596)</u>	<u>\$ —</u>	<u>\$ 54,777</u>	<u>\$159,949</u>

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

EDUCATION MANAGEMENT CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. OWNERSHIP AND OPERATIONS:

Education Management Corporation (“EDMC” or the “Company”) is among the largest providers of proprietary postsecondary education in the United States, based on student enrollment and revenues. Through its operating units, primarily The Art Institutes (“The Art Institutes”), the Company offers bachelor’s and associate’s degree programs and non-degree programs in the areas of design, media arts, culinary arts, fashion and paralegal studies. The Company has provided career-oriented education programs for over 35 years.

As of June 30, 2001, EDMC operated 24 schools in 20 major metropolitan areas throughout the United States. The Company’s main operating unit, The Art Institutes, offers programs designed to provide the knowledge and skills necessary for entry-level employment in various fields, including graphic design, media arts & animation, multimedia & web design, video production, interior design, industrial design, culinary arts, photography, and fashion. Those programs typically are completed in 18 to 48 months and culminate in a bachelor’s or associate’s degree. As of June 30, 2001, 19 Art Institutes offered bachelor’s degree programs.

As of June 30, 2001, the Company offered a culinary arts curriculum at 11 Art Institutes and The New York Restaurant School (“NYRS”), a culinary arts and restaurant management school located in New York City. NYRS offers an associate’s degree program and certificate programs.

NCPT (The National Center for Paralegal Training) offers paralegal certificate programs. The National Center for Professional Development maintained consulting relationships with certain colleges and universities to assist in the development, marketing and delivery of paralegal, legal nurse consultant and financial planning certificate programs. As of June 30, 2001, all but one of these relationships had expired or had been terminated, and the remaining expired on August 31, 2001.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Basis of Consolidation and Presentation

The consolidated financial statements include the accounts of Education Management Corporation and its subsidiaries. The results of operations of acquired entities are consolidated with those of the Company from the date of acquisition. All significant intercompany transactions and balances have been eliminated. The Company operates as one reportable segment in accordance with the manner in which it makes operating decisions and assesses performance.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from these estimates.

Government Regulations

The Art Institutes and NYRS (“the participating schools”) participate in various federal student financial assistance programs (“Title IV Programs”) under Title IV of the Higher Education Act of 1965, as amended (the “HEA”). Approximately 60% of the Company’s net revenues in 2001 were indirectly derived from funds distributed under these programs to students at the participating schools.

The participating schools are required to comply with certain federal regulations established by the U.S. Department of Education. Among other things, they are required to classify as restricted certain Title IV Program

funds in excess of charges currently applicable to students' accounts. Such funds are reported as restricted cash in the accompanying consolidated balance sheets.

The participating schools are required to administer Title IV Program funds in accordance with the HEA and U.S. Department of Education regulations and must use due diligence in approving and disbursing funds and servicing loans. In the event a participating school does not comply with federal requirements or if student loan default rates are at a level considered excessive by the federal government, that school could lose its eligibility to participate in Title IV Programs or could be required to repay funds determined to have been improperly disbursed. Management believes that the participating schools are in substantial compliance with the federal requirements and that student loan default rates are not at a level considered to be excessive.

Certain Art Institutes make contributions to Federal Perkins Loan Programs (the "Funds"). Current contributions to the Funds are made 75% by the federal government and 25% by the school. The Company carries its investments in the Funds at cost, net of an allowance for estimated future loan losses.

Cash and Cash Equivalents

The Company considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents. These investments are stated at cost which, based upon the scheduled maturities, approximates market value.

U.S. Department of Education regulations require Title IV Program funds received by the Company's schools in excess of the tuition and fees owed by the relevant students at that time to be, with these students' permission, maintained and classified as restricted until the students are billed for the portion of their education program related to those funds. Funds transferred through electronic funds transfer programs are held in a separate cash account and released when certain conditions are satisfied. These restrictions have not significantly affected the Company's ability to fund daily operations.

Inventories

Inventories consist mainly of textbooks, art supply kits, and supplies held for sale to students enrolled in the Company's educational programs. Inventories are valued at the lower of cost (first-in, first-out) or market.

Acquisitions

On October 1, 1998, the Company acquired the assets of Socrates Distance Learning Technologies Group for approximately \$500,000 in cash. This acquisition was made to further the development of the Company's distance learning capabilities.

On August 17, 1999, the Company acquired the outstanding stock of the American Business & Fashion Institute in Charlotte, North Carolina, for \$500,000 in cash. The school was renamed The Art Institute of Charlotte.

On August 26, 1999, the Company acquired the outstanding stock of Massachusetts Communications College in Boston, Massachusetts for approximately \$7.2 million in cash. Subsequent to June 30, 2001, the school was renamed The New England Institute of Art and Communications.

On October 13, 2000, the Company acquired the outstanding stock of The Art Institute of California in San Diego, California for approximately \$9.8 million in cash.

On April 11, 2001, the Company acquired the outstanding stock of the Design Institute located in Las Vegas, Nevada for approximately \$2.1 million in cash. The school was renamed The Art Institute of Las Vegas.

These acquisitions were accounted for using the purchase method of accounting, with the excess of the purchase price over the fair value of the assets acquired being assigned to identifiable intangible assets and goodwill. The results of the acquired entities have been included in the Company's results from the respective dates of acquisition. The pro forma effects, individually and collectively, of the acquisitions in the Company's consolidated financial statements would not materially impact the reported results.

Intangible Assets

Intangible assets consisted of the following:

	<u>As of June 30,</u>	
	<u>2000</u>	<u>2001</u>
	(in thousands)	
Goodwill, net of accumulated amortization of \$5,211 and \$6,221 (10 to 40 years)	\$26,588	\$36,918
Accreditation, curriculum and other, net of accumulated amortization of \$854 and \$1,821 (3 to 22 years)	<u>3,480</u>	<u>6,140</u>
	<u>\$30,068</u>	<u>\$43,058</u>

Lease Arrangements

The Company conducts a major part of its operations from leased facilities. In addition, the Company leases a portion of its furniture and equipment. In those cases in which the lease term approximates the useful life of the leased asset or the lease meets certain other prerequisites, the leasing arrangement is classified as a capitalized lease. The remaining lease arrangements are treated as operating leases.

Property and Equipment

Property and equipment are stated at cost, net of accumulated depreciation. Expenditures for additions and major improvements are capitalized, while those for maintenance, repairs and minor renewals are expensed as incurred. The Company uses the straight-line method of depreciation for financial reporting, while using different methods for tax purposes. Depreciation is based upon estimated useful lives, ranging from 3 to 30 years. Leasehold improvements are amortized over the term of the lease, or over their estimated useful lives, whichever is shorter.

Financial Instruments

The fair values and carrying amounts of the Company's financial instruments, primarily accounts receivable and debt, are approximately equivalent. The debt instruments bear interest at floating rates based upon market rates or at fixed rates that approximate market rates. All other financial instruments are classified as current and will be utilized within the next operating cycle.

Revenue Recognition and Receivables

The Company's net revenues consist of tuition and fees, student housing charges and supply store and restaurant sales. In fiscal 2001, the Company derived 89.8% of its net revenues from tuition and fees paid by, or on behalf of, its students. Net revenues, as presented, are reduced for student refunds and scholarships. Student supply store and restaurant sales are recognized as they occur. Advance payments represent that portion of payments received but not earned and are reflected as a current liability in the accompanying consolidated balance sheets.

The Company recognizes tuition and housing revenues on a monthly pro rata basis over the term of instruction, typically an academic quarter. For most Art Institute programs, the academic and financial quarters are the same; therefore unearned revenue is not significant at the end of a financial quarter. However, certain recently acquired schools have programs that have class starting and ending dates that differ from the financial

quarters. Revenue associated with tuition and certain fees is either recognized within the fiscal quarter to which the applicable service was rendered, or is deferred over the appropriate period. Unearned tuition revenue of approximately \$446,000 and \$1.7 million, related to programs not on the Company's traditional academic quarters, is included with advanced payments in the accompanying consolidated balance sheets as of June 30, 2000 and June 30, 2001, respectively. The Company's revenue recognition policies are in accordance with the Securities and Exchange Commission issued Staff Accounting Bulletin No. 101 "Revenue Recognition in Financial Statements."

Refunds are calculated in accordance with federal, state and accrediting agency standards. Student refunds of approximately \$8.6 million and \$8.9 million were recorded for 2000 and 2001, respectively, of which approximately \$168,000 and \$75,000 are included with accrued liabilities in the accompanying consolidated balance sheets as of June 30, 2000 and 2001, respectively.

The trade receivable balances are comprised of individually insignificant amounts due primarily from students throughout the United States. The Company determines its allowance for doubtful accounts by categorizing gross receivables based upon the enrollment status of the student (in-school, out of school, summer leave of absence and collections) and establishing a reserve based on the likelihood of collections (in-school receivables being the lowest percent reserved).

Costs and Expenses

Educational services expense consists primarily of costs related to the development, delivery and administration of the Company's education programs. Major cost components are faculty compensation, administrative salaries, costs of educational materials, facility leases and school occupancy costs, information systems costs and bad debt expense, along with depreciation and amortization of property and equipment.

General and administrative expense consists of marketing and student admissions expenses and certain central staff departmental costs such as executive management, finance and accounting, legal, corporate development and other departments that do not provide direct services to the Company's students. All advertising costs are expensed in the fiscal year incurred.

Amortization of intangibles relates primarily to the values assigned to identifiable intangibles and goodwill, which arose principally from the acquisitions discussed above. These intangible assets are amortized over periods ranging from 2 to 40 years.

New Accounting Standards

In June 2001, Statement of Financial Accounting Standard (SFAS) No. 141, "Business Combinations," was issued. The statement addresses financial accounting and reporting for business combinations and supersedes APB Opinion No. 16, "Business Combinations," and FASB statement No. 38 "Accounting for Preacquisition Contingencies of Purchased Enterprises." The statement requires that all business combinations initiated after June 30, 2001 be accounted for using the purchase method. SFAS 141 is effective July 1, 2001. The Company's adoption of SFAS 141 will not have a material impact on the Company's financial position or results of operations.

In June 2001, SFAS No. 142 "Goodwill and Other Intangible Assets," was issued. This Statement addresses financial accounting and reporting for acquired goodwill and other intangible assets and supersedes Accounting Pronouncement Bulletin (APB) Opinion No. 17, "Intangible Assets". It addresses how intangible assets that are acquired individually or with a group of other assets should be accounted for in financial statements upon their acquisition. This Statement also addresses how goodwill and other intangible assets should be accounted for after they have been initially recognized in the financial statements. The Company has adopted this standard as of July 1, 2001. The Company is required to complete a transitional goodwill impairment test for all goodwill at the reporting unit level by December 31, 2001 and is currently preparing for this. Adopting SFAS 142 will affect

the financial position and results of operations because goodwill will no longer be amortized. It is anticipated that the adoption of this standard in fiscal 2002 will decrease amortization of intangibles expense by approximately \$1 million, reduce the effective tax rate (but not the tax provision) by less than 1%, and increase diluted earnings per share by approximately \$.03 for the fiscal year.

Supplemental Disclosures of Cash Flow Information

	Year ended June 30,		
	1999	2000	2001
	(in thousands)		
Cash paid during the period for:			
Interest (net of amount capitalized)	\$ 313	\$ 175	\$ 2,485
Income taxes	13,846	15,590	11,494
Noncash investing and financing activities:			
Expenditures for property and equipment included in			
accounts payable	5,071	13,161	4,506
Tax benefit for options exercised	2,664	928	9,775

Reclassifications

Certain prior year balances have been reclassified to conform to the current year presentation.

3. SHAREHOLDERS' INVESTMENT:

Pursuant to the Company's Preferred Share Purchase Rights Plan (the "Rights Plan"), one Preferred Share Purchase Right (a "Right") is associated with each outstanding share of Common Stock. Each Right entitles its holder to buy one two-hundredth of a share of Series A Junior Participating Preferred Stock, \$.01 par value, at an exercise price of \$50, subject to adjustment (the "Purchase Price"). The Rights Plan is not subject to shareholder approval.

The Rights will become exercisable under certain circumstances following a public announcement by a person or group of persons (an "Acquiring Person") that they acquired or commenced a tender offer for 17.5% or more of the outstanding shares of Common Stock. If an Acquiring Person acquires 17.5% or more of the Common Stock, each Right will entitle its holder, except the Acquiring Person, to acquire upon exercise a number of shares of Common Stock having a market value of two times the Purchase Price. In the event that the Company is acquired in a merger or other business combination transaction or 50% or more of its consolidated assets or earning power are sold after a person or group of persons becomes an Acquiring Person, each Right will entitle its holder to purchase, at the Purchase Price, that number of shares of the acquiring company having a market value of two times the Purchase Price. The Rights will expire on the tenth anniversary of the closing of the IPO (fiscal 2007) and are subject to redemption by the Company at \$.01 per Right, subject to adjustment.

4. EARNINGS PER SHARE:

Basic EPS is computed using the weighted average number of shares actually outstanding during the period, while diluted EPS is calculated to reflect the potential dilution related to stock options.

Reconciliation of Diluted Shares

	Year ended June 30,		
	1999	2000	2001
	(in thousands)		
Basic shares	29,314	28,964	29,742
Dilution for stock options	1,301	957	1,274
Diluted shares	<u>30,615</u>	<u>29,921</u>	<u>31,016</u>

Options to purchase 122,181 and 7,280 shares were excluded from the dilutive earnings per share calculation because of their antidilutive effect (due to the exercise price of such options exceeding the average market price for the period) for fiscal years 2000 and 2001, respectively.

5. PROPERTY AND EQUIPMENT:

Property and equipment consisted of the following as of June 30:

	<u>2000</u>	<u>2001</u>
	(in thousands)	
Assets (asset lives in years)		
Land	\$ 4,300	\$ 4,300
Buildings and improvements (15 to 30)	29,351	51,698
Equipment and furniture (3 to 10)	123,165	136,442
Library books (3)	3,730	4,979
Leasehold interests and improvements (1 to 20)	55,554	60,359
Construction in progress	<u>19,707</u>	<u>3,064</u>
Total	235,807	260,842
Less accumulated depreciation	<u>101,069</u>	<u>111,360</u>
	<u>\$134,738</u>	<u>\$149,482</u>

6. LONG-TERM DEBT:

The Company and its subsidiaries were indebted under the following obligations as of June 30:

	<u>2000</u>	<u>2001</u>
	(in thousands)	
Revolving credit facilities	\$64,150	\$53,525
Other indebtedness	<u>133</u>	<u>135</u>
	64,283	53,660
Less current portion	<u>16</u>	<u>26</u>
	<u>\$64,267</u>	<u>\$53,634</u>

The Credit Agreement provides for maximum borrowings of \$100 million through its expiration on February 18, 2005. Borrowings under this facility are unsecured and bear interest at one of three rates set forth in the Credit Agreement, at the election of the Company. As of June 30, 2001, the average interest rate for borrowings under the Credit Agreement was 4.9%. Certain outstanding letters of credit reduce this facility. The Credit Agreement contains customary covenants that, among other matters, require the Company to meet specified interest and leverage ratio requirements, restrict the repurchase of Common Stock and the incurrence of additional indebtedness. As of June 30, 2001, the Company was in compliance with all covenants under the Credit Agreement.

Relevant information regarding borrowings under the revolving credit facilities under both the Credit Agreement and the prior borrowing agreement is reflected below:

	<u>Year ended June 30,</u>		
	<u>1999</u>	<u>2000</u>	<u>2001</u>
	(in thousands)		
Outstanding borrowings, end of period	\$36,500	\$64,150	\$53,525
Approximate average outstanding balance throughout the period	2,550	15,215	28,048
Approximate maximum outstanding balance during the period	37,000	79,850	64,150
Weighted average interest rate for the period	7.48%	7.45%	6.73%

Subsequent to June 30, 2001, the Company and its lenders amended and restated the Credit Agreement (See Note 14) to provide additional borrowing availability.

7. COMMITMENTS AND CONTINGENCIES:

The Company and its subsidiaries lease certain classroom, dormitory and office space under operating leases, which expire on various dates through September 2020. Rent expense under these leases was approximately \$28,250,000, \$33,645,000, and \$41,054,000 respectively for 1999, 2000 and 2001. The approximate minimum future commitments under non-cancelable, long-term operating leases as of June 30, 2001 are reflected below:

<u>Fiscal Years</u>	<u>(in thousands)</u>
2002	\$ 41,241
2003	34,623
2004	32,277
2005	31,302
2006	30,555
Thereafter	<u>183,892</u>
	<u>\$353,890</u>

The Company has a management incentive compensation plan that provides for the awarding of cash bonuses to management personnel using formalized guidelines based upon the operating results of each subsidiary and the Company.

The Company is a defendant in certain legal proceedings arising out of the conduct of its businesses. In the opinion of management, based upon its investigation of these claims and discussion with legal counsel, the ultimate outcome of such legal proceedings, individually and in the aggregate, will not have a material adverse effect on the consolidated financial position, results of operations or liquidity of the Company.

8. RELATED PARTY TRANSACTIONS:

The Art Institute of Philadelphia, a division of The Art Institutes International, Inc (“Aii”), itself a wholly-owned subsidiary of EDMC, leases one of the buildings it occupies from a partnership in which the subsidiary serves as a 1% general partner and an executive officer/director and a director of EDMC are minority limited partners. The Art Institute of Fort Lauderdale, Inc., a wholly-owned subsidiary of Aii, leases part of its facilities from a partnership in which an executive officer/director of EDMC is a minority limited partner. Total rental payments under these arrangements were approximately \$1,901,000, \$2,214,000, and \$2,267,000 for the years ended June 30, 1999, 2000, and 2001, respectively.

9. EMPLOYEE BENEFIT PLANS:

The Company sponsors a retirement plan that covers substantially all employees. This plan provides for matching Company contributions of 100% of employee 401(k) contributions up to 3% of compensation and 50% of contributions between 4% and 6% of compensation. Other contributions to the plan are at the discretion of the Board of Directors. The expense relating to these plans was approximately \$2,198,000, \$1,181,000, and \$1,939,000 for the years ended June 30, 1999, 2000, and 2001, respectively.

The Company’s retirement plan includes an ESOP, which enables eligible employees to have stock ownership in the Company. The ESOP provides for the allocations of forfeited shares and cash to be made to the accounts of eligible participating employees based upon each participant’s compensation level relative to the total compensation of all eligible employees. Eligible employees vest their ESOP accounts based on a five-year schedule, which includes credit for past service. Distribution of shares from the ESOP is made following the

retirement, disability or death of an employee. For employees who terminate for any other reason, their vested balance will be offered for distribution in accordance with the terms of the ESOP.

10. DEFERRED INCOME TAXES AND OTHER LONG-TERM ASSETS:

Deferred income taxes and other long-term assets consist of the following as of June 30:

	<u>2000</u>	<u>2001</u>
	(in thousands)	
Investment in Federal Perkins Loan Program, net of allowance for estimated future loan losses of \$1,209 and \$1,252	\$2,819	\$2,918
Cash value of life insurance, net of loans of \$781 each year; face value of \$6,065	2,620	2,935
Deferred income taxes	2,046	2,067
Other	1,671	1,670
	<u>\$9,156</u>	<u>\$9,590</u>

11. ACCRUED LIABILITIES:

Accrued liabilities consist of the following as of June 30:

	<u>2000</u>	<u>2001</u>
	(in thousands)	
Payroll taxes and payroll related	\$ 7,714	\$10,052
Income and other taxes	404	640
Other	4,944	4,000
	<u>\$13,062</u>	<u>\$14,692</u>

12. INCOME TAXES:

The provision for income taxes includes current and deferred taxes as reflected below:

	<u>Year ended June 30,</u>		
	<u>1999</u>	<u>2000</u>	<u>2001</u>
	(in thousands)		
Current taxes:			
Federal	\$11,824	\$14,020	\$18,129
State	3,227	2,961	3,021
Total current taxes	<u>15,051</u>	<u>16,981</u>	<u>21,150</u>
Deferred taxes	<u>(1,992)</u>	<u>(1,895)</u>	<u>(2,728)</u>
Total provision	<u>\$13,059</u>	<u>\$15,086</u>	<u>\$18,422</u>

The provision for income taxes reflected in the accompanying consolidated statements of income vary from the amounts that would have been provided by applying the federal statutory income tax rate to earnings before income taxes as shown below:

	<u>Year ended June 30,</u>		
	<u>1999</u>	<u>2000</u>	<u>2001</u>
Federal statutory income tax rate	35.0%	35.0%	35.0%
State and local income taxes, net of federal income tax benefit	4.9	4.4	3.7
Amortization of goodwill and other intangibles5	.4	.5
Nondeductible expenses7	.4	.2
Other, net	—	(.1)	(.5)
Effective income tax rate	<u>41.1%</u>	<u>40.1%</u>	<u>38.9%</u>

Net deferred income tax assets (liabilities) consist of the following as of June 30:

	<u>1999</u>	<u>2000</u>	<u>2001</u>
	(in thousands)		
Deferred income tax—current	\$2,476	\$2,872	\$4,946
Deferred income tax—long term	<u>548</u>	<u>2,046</u>	<u>2,067</u>
Net deferred income tax asset	<u>\$3,024</u>	<u>\$4,918</u>	<u>\$7,013</u>
Consisting of:			
Allowance for doubtful accounts	\$3,850	\$5,649	\$6,766
Assigned asset values in excess of tax basis	(1,585)	(1,767)	(1,640)
Depreciation	1,508	1,687	1,295
Financial reserves and other	<u>(749)</u>	<u>(651)</u>	<u>592</u>
Net deferred income tax asset	<u>\$3,024</u>	<u>\$4,918</u>	<u>\$7,013</u>

13. STOCK-BASED COMPENSATION:

The Company maintains a Stock Incentive Plan for directors, executive management and key personnel, which provides for the issuance of stock-based incentive awards with respect to a maximum of 5,000,000 shares of Common Stock. Options issued to employees under this plan provide for time-based vesting over four years.

The Company also has two non-qualified management stock option plans under which options to purchase a maximum of 1,119,284 shares of Common Stock were granted to management employees prior to 1996. All outstanding options under these non-qualified plans are fully vested. Under the terms of the three plans, the Board of Directors granted options to purchase shares at prices varying from \$1.27 to \$32.00 per share, representing the fair market value at the time of the grant.

The Company also has an employee stock purchase plan. The plan allows eligible employees of the Company to purchase up to an aggregate of 1,500,000 shares of Common Stock at quarterly intervals through periodic payroll deduction. The number of shares of Common Stock issued under this plan was 37,620, 59,800, and 31,712 in 1999, 2000 and 2001, respectively.

The Company accounts for these plans under Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." Had compensation expense for the stock option and stock purchase plans been determined consistent with SFAS No. 123, "Accounting for Stock-Based Compensation," the Company's net income and earnings per share would have been reduced to the following pro forma amounts:

		<u>1999</u>	<u>2000</u>	<u>2001</u>
Net income (in 000's):	As reported	\$18,752	\$22,530	\$28,978
	Pro forma	\$16,850	\$19,421	\$25,402
Basic EPS:	As reported	\$.64	\$.78	\$.97
	Pro forma	\$.57	\$.67	\$.85
Diluted EPS:	As reported	\$.61	\$.75	\$.93
	Pro forma	\$.55	\$.65	\$.82

Summary of Stock Options

	1999		2000		2001	
	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price
Outstanding, beginning of year	2,110,240	\$ 5.21	2,872,653	\$ 10.11	3,768,991	\$ 10.25
Granted	1,372,523	15.54	1,253,500	9.47	262,000	29.74
Exercised	544,610	4.42	270,392	4.44	1,352,519	8.12
Forfeited	65,500	13.29	86,770	12.72	110,498	11.47
Outstanding, end of year	<u>2,872,653</u>	<u>\$10.11</u>	<u>3,768,991</u>	<u>\$ 10.25</u>	<u>2,567,974</u>	<u>\$ 13.30</u>
Exercisable, end of year	<u>1,031,753</u>		<u>1,403,885</u>		<u>1,122,932</u>	
Weighted average fair value of options granted*	<u>\$ 7.97</u>		<u>\$ 5.58</u>		<u>\$ 17.54</u>	

Range of Exercise Prices	Options Outstanding			Options Exercisable		
	Options	Weighted-Average Remaining Contractual Life (years)	Weighted-Average Exercise Price	Options	Weighted-Average Exercise Price	
\$ 1.75—\$ 1.75	12,000	1.00	\$ 1.75	12,000	\$ 1.75	
2.85— 3.60	78,028	2.56	2.98	78,028	2.98	
7.50— 9.38	1,252,246	7.75	8.97	522,679	8.40	
12.38— 18.50	965,200	7.27	15.38	503,475	15.33	
19.38— 28.00	17,500	7.63	21.35	6,750	19.38	
30.13— 32.00	243,000	9.37	30.68	—	—	
	<u>2,567,974</u>	<u>7.53</u>	<u>\$13.30</u>	<u>1,122,932</u>	<u>\$11.12</u>	

* The fair value of each option granted is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions for grants:

	1999	2000	2001
Risk-free interest rate	4.97%	6.45%	5.79%
Expected dividend yield	0	0	0
Expected life of options (years)	6	6	6
Expected volatility rate	46.0%	55.0%	56.0%

14. SUBSEQUENT EVENTS — (UNAUDITED):

Subsequent to June 30, 2001, the following transactions occurred:

On July 9, 2001, the Company signed a merger agreement with Argosy Education Group, Inc., a leading provider of postgraduate professional education, headquartered in Chicago, IL. The merger agreement states that EDMC will acquire all of the shares of Argosy for \$12.00 cash per share for the approximately 6.5 million shares outstanding. This transaction is expected to close by the end of calendar year 2001 and is subject to obtaining certain regulatory approvals.

On July 25, 2001, the Company signed a purchase agreement acquiring the assets of The International Fine Arts College located in Miami, Florida. This transaction closed on September 5, 2001 (subject to final approval from the Department of Education).

On September 17, 2001, the Company signed an agreement to purchase certain assets of ITI Education Corporation (ITI), based in Halifax, Nova Scotia, Canada. This transaction is expected to close by the end of calendar year 2001 and is subject to obtaining certain regulatory approvals.

The acquisition of these entities will be accounted for in accordance with SFAS 141.

The Company and its lenders amended and restated the Credit Agreement, effective September 20, 2001, to increase allowable borrowings from \$100 million to \$200 million. The Amended and Restated Credit Agreement, which will expire September 20, 2004, is secured by certain assets of the Company and provides the Company the ability to borrow up to \$150 million on a revolving basis and \$50 million in the form of a term loan (collectively, the "Secured Credit Facilities"). The Secured Credit Facilities contain the customary covenants that, among other matters, require the Company to meet specified financial ratios, restrict the repurchase of Common Stock and limit the incurrence of additional indebtedness.

ITEM 9—CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Not applicable.

PART III

ITEM 10—DIRECTORS AND EXECUTIVE OFFICERS OF THE COMPANY

The information required by this Item will be contained in the Proxy Statement under the captions “Nominees as Directors for Terms Expiring at the 2004 Annual Meeting of Shareholders,” “Directors Continuing in Office,” “Executive Officers of the Company,” and “Section 16(a) Beneficial Ownership Reporting Compliance,” and is incorporated herein by reference.

ITEM 11—EXECUTIVE COMPENSATION

The information required by this Item will be contained in the Proxy Statement under the captions “Compensation of Executive Officers,” “Directors’ Compensation,” “Compensation Committee Interlocks and Insider Participants” and “Employment Agreements,” and is incorporated herein by reference.

ITEM 12—SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The information required by this Item will be contained in the Proxy Statement under the caption “Security Ownership,” and is incorporated herein by reference.

ITEM 13—CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information required by this Item will be contained in the Proxy Statement under the caption “Certain Transactions,” and is incorporated herein by reference.

PART IV

ITEM 14—EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

(a) The exhibits listed on the Exhibit Index on pages E-1 and E-2 of this Form 10-K are filed herewith or are incorporated herein by reference.

(1) Financial Statements:

The following financial statements of the Company and its subsidiaries are included in Part II, Item 8, on pages 24 through 39 of this Form 10-K.

Report of Independent Public Accountants

Consolidated Balance Sheets for years ended June 30, 2000 and 2001

Consolidated Statements of Income for years ended June 30, 1999, 2000 and 2001

Consolidated Statements of Cash Flows for years ended June 30, 1999, 2000 and 2001

Consolidated Statements of Shareholders' Investment for years ended June 30, 1999, 2000 and 2001

Notes to Consolidated Financial Statements

(2) Supplemental Financial Statement Schedules

Valuation and Qualifying Accounts, on page S-1 of this Form 10-K, is filed herewith.

(b) No reports on Form 8-K were filed during the three months ended June 30, 2001.

SIGNATURES

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

EDUCATION MANAGEMENT CORPORATION

By: /s/ ROBERT B. KNUTSON

Robert B. Knutson
Chairman and Chief Executive Officer

Date: September 28, 2001

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

<u>Signatures</u>	<u>Title</u>	<u>Date</u>
<u>S/ ROBERT B. KNUTSON</u> Robert B. Knutson	Chairman and Chief Executive Officer; Director	September 28, 2001
<u>S/ ROBERT P. GIOELLA</u> Robert P. Gioella	President and Chief Operating Officer; Director	September 28, 2001
<u>S/ JOHN R. MCKERNAN, JR.</u> John R. McKernan, Jr.	Vice Chairman; Director	September 28, 2001
<u>S/ ROBERT T. MCDOWELL</u> Robert T. McDowell	Executive Vice President and Chief Financial Officer	September 28, 2001
<u>S/ ROBERT H. ATWELL</u> Robert H. Atwell	Director	September 28, 2001
<u>S/ JAMES J. BURKE, JR.</u> James J. Burke, Jr.	Director	September 28, 2001
<u>S/ WILLIAM M. CAMPBELL, III</u> William M. Campbell, III	Director	September 28, 2001
<u>S/ ALBERT GREENSTONE</u> Albert Greenstone	Director	September 28, 2001
<u>S/ MIRYAM L. KNUTSON</u> Miryam L. Knutson	Director	September 28, 2001
<u>S/ JAMES S. PASMAN, JR.</u> James S. Pasman, Jr.	Director	September 28, 2001
<u>S/ DANIEL M. FITZPATRICK</u> Daniel M. Fitzpatrick	Vice President and Controller	September 28, 2001

EXHIBIT INDEX

<u>Exhibit Number</u>	<u>Exhibit</u>	<u>Method of Filing</u>
3.01	Amended and Restated Articles of Incorporation	Incorporated herein by reference to Exhibit 3.01 to the Annual Report on Form 10-K for the year ended June 30, 1997 (the “1997 Form 10-K”)
3.02	Articles of Amendment filed on February 4, 1997	Incorporated herein by reference to Exhibit 3.02 to the 1997 Form 10-K
3.03	Restated By-laws	Incorporated herein by reference to Exhibit 3.03 to the 1997 Form 10-K
4.01	Specimen Common Stock Certificate	Incorporated herein by reference to Exhibit 4.01 to Amendment No. 3 filed on October 28, 1996 to the Registration Statement on Form S-1 (File No. 333-10385) filed on August 19, 1996 (the “Form S-1”)
4.02	Rights Agreement, dated as of October 1, 1996, between Education Management Corporation and Mellon Bank, N.A	Incorporated herein by reference to Exhibit 4.02 to the 1997 Form 10-K
4.03	Amendment No. 1, dated November 9, 1999, to the Rights Agreement dated as of October 1, 1996 between the Company and ChaseMellon Shareholder Services, L.L.C., as Rights Agent	Incorporated herein by reference to Exhibit 4.01 to Quarterly Report on Form 10-Q for the quarter ended September 30, 1999 (the “September 30, 1999 10-Q”)
4.04	Letter Agreement dated November 9, 1999 by and among the Company, Baron Capital Group, Inc., BAMCO, Inc., Baron Capital Management Inc. and Ronald Baron	Incorporated herein by reference to Exhibit 4.02 to the September 30, 1999 10-Q
4.05	Credit Agreement, dated February 18, 2000, among Education Management Corporation, certain banks, National City Bank of Pennsylvania and First Union National Bank	Incorporated herein by reference to Exhibit 4.01 to Quarterly Report on Form 10-Q for the quarter ended March 31, 2000 (the “March 31, 2000 Form 10-Q”)
4.06	First Amendment to Credit Agreement, dated March 31, 2000 among Education Management Corporation, certain banks, National City Bank of Pennsylvania and First Union National Bank	Incorporated herein by reference to Exhibit 4.02 to the March 2000 Form 10-Q
10.01	Education Management Corporation Retirement Plan, amended and restated as of August 1, 2001	Filed herewith*
10.02	Education Management Corporation Management Incentive Stock Option Plan, effective November 11, 1993	Incorporated herein by reference to Exhibit 10.05 to the Form S-1*

<u>Exhibit Number</u>	<u>Exhibit</u>	<u>Method of Filing</u>
10.03	EMC Holdings, Inc. Management Incentive Stock Option Plan, effective July 1, 1990	Incorporated herein by reference to Exhibit 10.06 to Amendment No. 1*
10.04	Form of Management Incentive Stock Option Agreement, dated various dates, between EMC Holdings, Inc. and various management employees	Incorporated herein by reference to Exhibit 10.07 to Amendment No. 1*
10.05	Form of Amendment to Management Incentive Stock Option Agreement, dated January 19, 1995, among Education Management Corporation and various management employees	Incorporated herein by reference to Exhibit 10.08 to Amendment No. 1*
10.06	Education Management Corporation Deferred Compensation Plan amended and restated as of April 1, 2000	Filed herewith*
10.07	1996 Employee Stock Purchase Plan	Incorporated herein by reference to Exhibit 10.12 to Amendment No. 1
10.08	Education Management Corporation 1996 Stock Incentive Plan	Incorporated herein by reference to Exhibit 10.13 to Amendment No. 1*
10.09	Third Amended and Restated Employment Agreement, dated as of September 8, 1999 between Robert B. Knutson and Education Management Corporation	Incorporated herein by reference to Exhibit 10.09 to the 1999 Form 10-K*
10.10	Form of Employment Agreement, dated as of June 4 and September 8, 1999, between certain executives and Education Management Corporation	Incorporated herein by reference to Exhibit 10.10 to the 1999 Form 10-K*
10.11	Form of EMC-Art Institutes International, Inc. Director's and/or Officer's Indemnification Agreement	Incorporated herein by reference to Exhibit 10.17 to the Form S-1
10.12	Senior Management Team Incentive Compensation Plan	Incorporated herein by reference to Exhibit 10.12 to the 1999 Form 10-K*
10.13	Common Stock Registration Rights Agreement, dated as of August 15, 1996, among Education Management Corporation and Marine Midland Bank, Northwestern Mutual Life Insurance Company, National Union Fire Insurance Company of Pittsburgh, PA, Merrill Lynch Employees LBO Partnership No. I, L.P., Merrill Lynch IBK Positions, Inc., Merrill Lynch KECALP L.P., 1986, Merrill Lynch Offshore LBO Partnership No. IV, Merrill Lynch Capital Corporation, Merrill Lynch Capital Appreciation Partnership IV, L.P., Robert B. Knutson and certain other individuals	Incorporated herein by reference to Exhibit 10.19 to the 1997 Form 10-K
21.01	Material subsidiaries of Education Management Corporation	Filed herewith
23.01	Consent of Arthur Andersen LLP	Filed herewith

* Management contract or compensatory plan or arrangement.

**REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS ON
FINANCIAL STATEMENT SCHEDULE**

We have audited in accordance with auditing standards generally accepted in the United States, the consolidated financial statements of Education Management Corporation and Subsidiaries included in this Form 10-K, and have issued our report thereon dated July 27, 2001. Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The schedule listed in Item 14(a)(2) of this Form 10-K is the responsibility of the Company's management and is presented for purposes of complying with the Securities and Exchange Commission's rules and is not part of the basic financial statements. This schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, fairly states in all material respects the financial data required to be set forth therein in relation to the basic financial statements taken as a whole.

s/ Arthur Andersen LLP

Pittsburgh, Pennsylvania
July 27, 2001

SCHEDULE II

EDUCATION MANAGEMENT CORPORATION AND SUBSIDIARIES

VALUATION AND QUALIFYING ACCOUNTS

(Dollars in thousands)

	<u>Balance at Beginning of Period</u>	<u>Additions Charged to Expenses</u>	<u>Deductions</u>	<u>Other(a)</u>	<u>Balance at End of Period</u>
Allowance accounts for:					
Year ended June 30, 1999					
Uncollectible accounts receivable	\$ 8,318	\$ 5,660	\$ 4,611	\$ —	\$ 9,367
Estimated future loan losses	1,032	123	—	—	1,155
Year ended June 30, 2000					
Uncollectible accounts receivable	\$ 9,367	\$ 7,551	\$ 2,986	\$ 156	\$ 14,088
Estimated future loan losses	1,155	54	—	—	1,209
Year ended June 30, 2001					
Uncollectible accounts receivable	\$ 14,088	\$ 9,250	\$ 6,109	\$ 181	\$ 17,410
Estimated future loan losses	1,209	43	—	—	1,252

(a) Allowance for uncollectible accounts receivable acquired in connection with acquisitions of subsidiaries.