

GLEN BURNIE BANCORP  
Form 10-K  
April 02, 2018  
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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 December 31, 2017 or

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from to

Commission file number: 0 24047

GLEN BURNIE BANCORP

(Exact name of registrant as specified in its charter)

MARYLAND (State or other jurisdiction of incorporation or organization)	52 1782444 (I.R.S. Employer Identification No.)
101 Crain Highway, S.E., Glen Burnie, Maryland (Address of principal executive offices)	21061 (Zip Code)
Registrant's telephone number, including area code	(410) 766 3300

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

Title of Class	Name of Each Exchange on Which Registered
None	None

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

Title of Class  
Common Stock,  
\$1.00 par value  
Common Stock  
Purchase Rights

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

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Yes No

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

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

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

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

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

Large Accelerated Filer Accelerated File Non-Accelerated Filer Smaller Reporting Company Emerging Growth Company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The aggregate market value of the registrant's outstanding common equity held by non-affiliates was \$23,553,580, computed by reference to the closing sales price of such equity as of the last business day of the registrant's most recently completed second fiscal quarter (June 30, 2017). For the purposes of this calculation, directors, executive officers, and the controlling investor are considered affiliates.

The number of shares of common stock outstanding as of March 23, 2018 was 2,804,456.

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Documents Incorporated By Reference

Portions of the registrant's definitive proxy statement for the 2018 Annual Meeting of Stockholders to be filed with the SEC pursuant to Regulation 14A are incorporated by reference into Part III of this Annual Report on Form 10-K.

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## GLEN BURNIE BANCORP

## 2017 ANNUAL REPORT ON FORM 10 K

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### PART I

As used in this Annual Report, the term “the Company” refers to Glen Burnie Bancorp and, unless the context clearly requires otherwise, the terms “we,” “us,” and “our,” refer to Glen Burnie Bancorp and its consolidated subsidiaries.

### ITEM 1. BUSINESS

#### GENERAL

Glen Burnie Bancorp (the “Company”) is a bank holding company organized in 1990 under the laws of the State of Maryland. The Company owns all the outstanding shares of capital stock of The Bank of Glen Burnie (the “Bank”), a commercial bank organized in 1949 under the laws of the State of Maryland, serving northern Anne Arundel County and surrounding areas from its main office and branch in Glen Burnie, Maryland and branch offices in Odenton, Riviera Beach, Crownsville, Severn (two locations), Linthicum and Severna Park, Maryland. The Bank also maintains a remote Automated Teller Machine (“ATM”) location in Pasadena, Maryland. The Bank maintains a website at [www.thebankofglenburnie.com](http://www.thebankofglenburnie.com). It is the oldest independent commercial bank in Anne Arundel County. The Bank is engaged in the commercial and retail banking business as authorized by the banking statutes of the State of Maryland, including the acceptance of demand and time deposits, and the origination of loans to individuals, associations, partnerships and corporations.

The Bank’s real estate financing consists of residential first and second mortgage loans, home equity lines of credit and commercial mortgage loans. Commercial lending consists of both secured and unsecured loans. The Bank also originates automobile loans through arrangements with local automobile dealers. The Bank’s deposits are insured up to applicable limits by the Federal Deposit Insurance Corporation (“FDIC”). We attract deposit customers from the general public and use such funds, together with other borrowed funds, to make loans. Our results of operations are primarily determined by the difference between interest incomes earned on our interest-earning assets, primarily interest and fee income on loans, and interest paid on our interest-bearing liabilities, including deposits and borrowings.

The Company’s principal executive office is located at 101 Crain Highway, S.E., Glen Burnie, Maryland 21061. Its telephone number at such office is (410) 766 3300.

The Company also owns all outstanding shares of capital stock of GBB Properties, Inc. (“GBB”), another Maryland corporation which was organized in 1994 and which is engaged in the business of acquiring, holding and disposing of real property, typically acquired in connection with foreclosure proceedings (or deeds in lieu of foreclosure) instituted by the Bank or acquired in connection with branch expansions by the Bank.

#### RECENT DEVELOPMENTS

On December 22, 2017, President Trump signed into law major tax legislation commonly referred to as the Tax Cuts and Jobs Act (“Tax Reform Act”). The Tax Reform Act reduces the U.S. federal corporate income tax rate from 35 percent to 21 percent and makes many other changes to the U.S. tax code. We were required to revalue our deferred tax assets and liabilities at the new statutory tax rate upon enactment. As a result of this revaluation, in 2017, we recognized a one-time \$0.6 million income tax expense.

#### AVAILABILITY OF INFORMATION

Information on the Company and its subsidiary Bank may be obtained from the Company’s website [www.thebankofglenburnie.com](http://www.thebankofglenburnie.com). Copies of the Company’s annual report on Form 10 K, quarterly reports on Form 10 Q,

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current reports on Form 8 K, and all amendments thereto are available free of charge on the website as soon as practicable after they are filed with the Securities and Exchange Commission (SEC) through a link to the SEC's EDGAR reporting system. Simply select the "Investor Relations" menu item, then click on the "All SEC Filings" or "Insider Transactions" link.

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### MARKET AREA

The Bank considers its principal market area for lending and deposit products to consist of Anne Arundel County, Maryland. Anne Arundel County includes the suburbs of the City of Baltimore and is characterized by an aging population. Management believes that the majority of the working population in its market area either commutes to Baltimore or is employed at businesses located at or around the nearby Baltimore Washington International Airport. Lending activities are broader, including the entire State of Maryland, and, to a limited extent, the surrounding states. All of our revenue is generated within the United States.

### COMPETITION

Our principal competitors for deposits are other financial institutions, including other savings institutions, commercial banks, credit unions, and local banks and branches or affiliates of other larger banks located in our primary market area. Competition among these institutions is based primarily on interest rates and other terms offered, service charges imposed on deposit accounts, the quality of services rendered, and the convenience of banking facilities. Additional competition for depositors' funds comes from mutual funds, U.S. Government securities, insurance companies and private issuers of debt obligations and suppliers of other investment alternatives for depositors such as securities firms. Competition from credit unions has intensified in recent years as historical federal limits on membership have been relaxed. Because federal law subsidizes credit unions by giving them a general exemption from federal income taxes, credit unions have a significant cost advantage over banks and savings associations, which are fully subject to federal income taxes. Credit unions may use this advantage to offer rates that are highly competitive with those offered by banks and thrifts.

The Bank's interest rates, loan and deposit terms, and offered products and services are impacted, to a large extent, by competition. With respect to indirect lending, the Bank faces competition from other banks and the financing arms of automobile manufacturers. We compete in this area by offering competitive rates and responsive service to dealers. The Bank attempts to provide superior service within its community and to know, and facilitate services, to, its customers. It seeks commercial relationships with small to medium size businesses, which the Bank believes would welcome personal service and flexibility. The Bank believes its greatest competition comes from larger intra- and inter-state financial institutions.

### STRATEGY

We operate on the premise that the consolidation activities in the banking industry have created an opportunity for a well-capitalized community bank to satisfy banking needs that are no longer being adequately met in the local market. Large national and regional banks are catering to larger customers and provide an impersonal experience, and typical community banks, because of their limited capacity, are unable to meet the needs of many small-to-medium-sized businesses. Specifically, as a result of bank mergers in the 1990s, many banks in the Baltimore metropolitan area became local branches of large regional and national banks. Although size gave the larger banks some advantages in competing for business from large corporations, including economies of scale and higher lending limits, we believe that these larger, national banks remain focused on a mass market approach which de-emphasizes personal contact and service. We also believe that the centralization of decision-making power at these large institutions has resulted in a lack of customer service. At many of these institutions, determinations are made at the out-of-state "home office" by individuals who lack personal contact with customers as well as an understanding of the customers' needs and scope of the relationship with the institution. We believe that this trend is ongoing, and continues to be particularly frustrating to owners of small and medium-sized businesses, business professionals and individual consumers who traditionally have been accustomed to dealing directly with a bank executive who had an understanding of their banking needs with the ability to deliver a prompt response.

We attempt to differentiate ourselves from the competition through personalized service, flexibility in meeting the needs of customers, prompt decision making and the availability of senior management to meet with customers and prospective customers.

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PRODUCTS AND SERVICES

General

Our primary market focus is on making loans to and gathering deposits from small and medium-sized businesses and their owners, professionals and executives, real estate investors and individual consumers in our primary market area. We lend to customers throughout Maryland, with our core market being Northern Anne Arundel County and surrounding areas of Central Maryland. To a limited extent, we lend to customers in neighboring states. The Bank offers a full range of consumer and commercial loans. The Bank's lending activities include residential and commercial real estate loans, construction loans, land acquisition and development loans, commercial loans and consumer installment lending including indirect automobile lending. Substantially all of the Bank's loan customers are residents of Anne Arundel County and surrounding areas of Central Maryland. The Bank solicits loan applications for commercial loans from small to medium sized businesses located in its market area. The Company believes that this is a market in which a relatively small community bank, like the Bank, has a competitive advantage in personal service and flexibility. The Bank's consumer lending currently consists primarily of indirect automobile loans originated through arrangements with local dealers.

Lending Activities

Credit Policies and Administration

The Bank's lending activities are conducted pursuant to written policies approved by the Board of Directors ("Board") intended to ensure proper management of credit risk. Loans are subject to a well-defined credit process that includes credit evaluation of borrowers, establishment of lending limits and application of lending procedures, including the holding of adequate collateral and the maintenance of compensating balances, as well as procedures for on-going identification and management of credit deterioration. Regular portfolio reviews are performed by the Bank's senior credit officer to identify potential underperforming loans and other credit facilities, estimate loss exposure and to ascertain compliance with the Bank's policies. For significant problem loans, management review consists of evaluation of the financial strengths of the borrower and any guarantor, the related collateral, and the effects of economic conditions.

The Bank's loan approval policy provides for various levels of individual lending authority. The maximum aggregate lending authority granted by the Bank to any one Lending Officer is \$750,000. A combination of approvals from certain officers may be used to lend up to an aggregate of \$1,000,000. We have adopted a comprehensive lending policy, which includes stringent underwriting standards for all types of loans. Our lending staff follows pricing guidelines established periodically by our management team. The Bank maintains two committees, separate from the Board of Directors, which have authorization to approve extensions of credit. The two committees are called the Officer's Loan Committee ("OLC") and the Executive Committee ("EC"). The OLC is authorized to approve extensions of credit where the total aggregate amount of credit to the borrower or guarantor is less than or equal to \$1,000,000. The OLC consists of the President/Chief Executive Officer ("President/CEO"), Chief Financial Officer ("CFO"), and Chief Lending Officer ("CLO") plus two additional loan officers. The EC approves extensions of credit where the aggregate amount of credit to an existing borrower is less than or equal to \$3,000,000. The EC is comprised of the Chairman of the Board, or the President/CEO plus two (2) outside Directors. Extensions of credit greater than \$3,000,000 must be approved by the Board of Directors. Under the leadership of our executive management team, we believe that we employ experienced lending officers, secure appropriate collateral and carefully monitor the financial conditions of our borrowers and the concentration of loans in our portfolio.

All loans by the Bank to our directors and executive officers and their affiliates require pre-approval by the Bank's Board of Directors to ensure, among other things, compliance with Section 23A and Section 23B of the Federal

Reserve Act and Regulation O promulgated thereunder. It is the Bank's policy that all approved loans must be made on substantially the same terms as loans made to persons who are unrelated to the Bank.

In addition to the normal repayment risks, all loans in the portfolio are subject to the state of the economy and the related effects on the borrower and/or the real estate market. Generally, longer-term loans have periodic interest rate

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adjustments and/or call provisions. Senior management monitors the loan portfolio closely to ensure that we minimize past due loans and that we swiftly deal with potential problem loans.

The Bank also retains an outside, independent firm to review the loan portfolio. This firm performs a detailed annual review. We use the results of the firm's report primarily to validate the risk ratings applied to loans in the portfolio and identify any systemic weaknesses in underwriting, documentation or management of the portfolio. Results of the annual review are presented to executive management, the audit committee of the board and the full board of directors and are available to and used by regulatory examiners when they review the Bank's asset quality.

The Bank maintains the normal checks and balances on the loan portfolio not only through the underwriting process but through the utilization of an internal credit administration group that both assists in the underwriting and serves as an additional reviewer of underwriting. The separately managed loan administration group also has oversight for documentation, compliance and timeliness of collection activities. Our internal audit department also reviews documentation, compliance and file management.

### Real Estate Lending

The Bank offers long-term mortgage financing for residential and commercial real estate as well as shorter term construction and land development loans. Residential mortgage and residential construction loans are originated with fixed rates, while commercial mortgages may be originated on either a fixed or variable rate basis. Commercial construction loans may be originated on either a fixed or a variable rate basis. Substantially all of the Bank's real estate loans are secured by properties in Anne Arundel County, Maryland. Under the Bank's loan policies, the maximum permissible loan-to-value ratio for owner-occupied residential mortgages is 80% of the lesser of the purchase price or appraised value. For residential investment properties, the maximum loan-to-value ratio is 80%. The maximum permissible loan-to-value ratio for residential and residential construction loans is 80%. The maximum loan-to-value ratio for permanent commercial mortgages is 75%. The maximum loan-to-value ratio for land development loans is 70% and for unimproved land is 65%. The Bank also offers home equity loans secured by the borrower's primary residence, provided that the aggregate indebtedness on the property does not exceed 80% of its value for loan commitments greater than \$100,000. Because mortgage lending decisions are based on conservative lending policies, the Company has no exposure to the credit issues affecting the sub-prime residential mortgage market.

Primary risks associated with residential real estate loans include fluctuating land and property values and rising interest rates with respect to fixed-rate, long-term loans. Residential construction lending exposes the Company to risks related to builder performance.

### Commercial Lending

The Bank's commercial loan portfolio consists of demand, installment and time loans for commercial purposes. The Bank's business demand, installment and time lending includes various working capital loans, equipment, vehicles, lines of credit and letters of credit for commercial customers. Demand loans require the payment of interest until called, while installment loans require a monthly payment of principal and interest, and time loans require at maturity a single payment of principal and interest due monthly. Such loans may be made on a secured or an unsecured basis. All such loans are underwritten on the basis of the borrower's creditworthiness rather than the value of the collateral.

The primary risks associated with commercial loans, including commercial real estate loans, are the quality of the borrower's management and a number of economic and other factors which induce business failures and depreciate the value of business assets pledged to secure the loan, including competition, insufficient capital, product obsolescence,

changes in the borrowers' cost, environmental hazards, weather, changes in laws and regulations and general changes in the marketplace.

#### Installment Lending

The Bank makes consumer and commercial installment loans for the purchase of automobiles, boats, other consumer durable goods, capital goods and equipment. Such loans provide for repayment in regular installments and

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are secured by the goods financed. Also included in installment loans are other types of credit repayable in installments. As of December 31, 2017, approximately 43% of the installment loans in the Bank's portfolio (other than indirect automobile lending) had been originated for commercial purposes and 57% had been originated for consumer purposes.

### Indirect Automobile Lending

The Bank commenced its indirect automobile lending program in January 1998. The Bank finances new and used automobiles for terms of no more than 72 months except for vehicles with original purchase prices greater than \$60,000 which may be written for terms up to 75 months if approved by a Senior Loan Officer, CLO, CFO, CEO, or President. The Bank will lend a maximum of 100% of invoice on new vehicles. On used vehicles, the Bank will not lend more than 90% of the of the average retail value as defined by a major national publication approved by the Bank. The Bank requires all borrowers to obtain vendor's single interest coverage protecting the Bank against loss in the case a borrower's automobile insurance lapses. The Bank originates indirect loans through a network of approximately 65 dealers which are primarily new car dealers located in Anne Arundel County and the surrounding counties. Participating dealers take loan applications from their customers and transmit them to the Bank for approval.

Indirect automobile loans, are affected primarily by domestic economic instability and a variety of factors that may lead to the borrower's unemployment, including deteriorating economic conditions in one or more segments of a local or broader economy. Because the Bank deals with borrowers through an intermediary on indirect automobile loans, this form of lending potentially carries greater risks of defects in the application process for which claims may be made against the Bank. Indirect automobile lending may also involve the Bank in consumer disputes under state "lemon" or other laws. The Bank seeks to control these risks by following strict underwriting and documentation guidelines. In addition, dealerships are contractually obligated to indemnify the Bank for such losses for a limited period of time.

### Consumer Lending

We offer various types of secured and unsecured consumer loans. Generally, our consumer loans are made for personal, family or household purposes as a convenience to our customer base. As a general guideline, a consumer's total debt service should not exceed 38% of their gross income. The underwriting standards for consumer loans include a determination of the applicant's payment history on other debts and an assessment of his or her ability to meet existing obligations and payments on the proposed loan.

Consumer loans may present greater credit risk than residential real estate loans because many consumer loans are unsecured or are secured by rapidly depreciating assets. Repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment of the outstanding loan balance because of the greater likelihood of damage, loss or depreciation. Consumer loan collections also depend on the borrower's continuing financial stability. If a borrower suffers personal financial difficulties, the loan may not be repaid. Also, various federal and state laws, including bankruptcy and insolvency laws, may limit the amount we can recover on such loans.

### Personal Unsecured Lines

The Bank offers overdraft protection lines of credit, tied to checking accounts, as a convenience to qualified customers.

### Loan Originations, Purchases, Sales, Participations and Servicing

All loans that we originate are underwritten pursuant to our policies and procedures, which incorporate standard underwriting guidelines. We originate both fixed and variable rate loans. Our loan origination activity may be adversely affected by a rising interest rate environment that typically results in decreased loan demand. We occasionally sell participations in commercial loans to correspondent banks if the amount of the loan exceeds our internal limits. More rarely, we purchase loan participations from correspondent banks in the local market as well. Those loans are underwritten in-house with the same standards as loans directly originated.

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Loan Approval Procedures and Authority

Our lending activities follow written, non-discriminatory underwriting standards and loan origination procedures established by our board of directors. The loan approval process is intended to assess the borrower's ability to repay the loan, the viability of the loan, and the adequacy of the value of the collateral that will secure the loan, if applicable. To assess a business borrower's ability to repay, we review and analyze, among other factors: current income, credit history including the Bank's prior experience with the borrower, cash flow, any secondary sources of repayment, other debt obligations in regards to the equity/net worth of the borrower and collateral available to the Bank to secure the loan.

We require appraisals or valuations of all real property securing one-to-four family residential and commercial real estate loans and home equity loans and lines of credit. All appraisers are state licensed or state certified appraisers, and a list of approved appraisers is maintained and updated on an annual basis.

Deposit Activities

Deposits are the major source of our funding. We offer a broad array of consumer and business deposit products that include demand, money market, and savings accounts, as well as time deposits. We offer a competitive array of commercial cash management products, which allow us to attract demand deposits. We believe that we pay competitive rates on our interest-bearing deposits. As a relationship-oriented organization, we generally seek to obtain deposit relationships with our loan clients.

Other Banking Products

We offer our customers treasury services products that include wire transfer and ACH services, checkcards and automated teller machines at most of our full service branch locations, safe deposit boxes at some full service locations and credit cards through asp; 5.00 5.00 5.00

Risk-free interest rate

3.87% 4.89% 3.77% 4.89%

Dividend yield

Expected volatility

33.73% 30.70% 34.47% 30.70%

Expected forfeiture rate

3.00% 3.00%

The following table summarizes restricted stock activity under the 2003 Plan for the nine months ended June 30, 2006.

	<b>Number of Shares</b>	<b>Weighted Average Grant Date Fair Value per Share</b>
Outstanding at September 30, 2005		\$
Awarded	117	\$ 23.25

Outstanding at June 30, 2006	117	\$	23.25
Non-vested restricted stock at June 30, 2006	117	\$	23.25

For the three and nine months ended June 30, 2006, our consolidated financial statements reflect the impact of SFAS No. 123(R). In accordance with the modified prospective transition method, which results in recognition of compensation expense for all stock option and other equity-based awards that vest or become exercisable after the effective date of adoption, our consolidated financial statements for prior periods have not been restated to reflect, and do not include the impact of, SFAS No. 123(R).

SFAS No. 123(R) requires us to estimate the fair value of share-based payment awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as expense over the period during which an employee is required to provide service in exchange for

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**UNIVERSAL TECHNICAL INSTITUTE, INC.**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**  
**(In thousands, except per share amounts)**

the award. Prior to the adoption of SFAS No. 123(R), we accounted for stock-based awards to employees using the intrinsic value method in accordance with APB No. 25 as allowed under SFAS No. 123.

Awards which vested in fiscal year 2005 and earlier were accounted for under the intrinsic value method prescribed in APB No. 25. For the three and nine months ended June 30, 2005, there was no stock compensation expense under ABP No. 25. If we had elected to recognize compensation expense based on the estimated fair value of the awards, estimated using the Black-Scholes option pricing model, at the grant date in accordance with SFAS No. 123, net earnings would have been the pro forma amounts shown as follows:

	<b>Three Months Ended June 30, 2005</b>	<b>Nine Months Ended June 30, 2005</b>
Net income available to common shareholders as reported	\$ 7,605	\$ 26,588
Add stock-based compensation expense included in reported net income, net of taxes	8	24
Deduct total stock-based employee compensation expense determined using the fair value based method, net of taxes	(718)	(1,714)
Net income pro forma	\$ 6,895	\$ 24,898
Earnings per share basic as reported	\$ 0.27	\$ 0.95
Earnings per share diluted as reported	\$ 0.27	\$ 0.93
Earnings per share basic pro forma	\$ 0.24	\$ 0.89
Earnings per share diluted pro forma	\$ 0.24	\$ 0.87

Stock-based compensation expense recognized for the three and nine months ended June 30, 2006 included compensation expense for share-based payment awards granted prior to, but not yet vested as of, September 30, 2005, based on the grant date fair value estimated in accordance with the pro forma provisions of SFAS No. 123. We recognize compensation expense using the straight-line single-option method. Stock-based compensation expense, recognized for the three and nine months ended June 30, 2006, is based on awards ultimately expected to vest, and accordingly it has been reduced for estimated forfeitures. SFAS No. 123(R) requires forfeitures to be estimated at the time of grant. Estimated forfeitures are revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. In our pro forma information required under SFAS No. 123 for the periods prior to fiscal 2006, we accounted for forfeitures as they occurred.

The following table summarizes the accounts in the accompanying condensed consolidated income statements where stock compensation expense under SFAS No. 123(R) has been recorded:

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**UNIVERSAL TECHNICAL INSTITUTE, INC.**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**  
(In thousands, except per share amounts)

	<b>Three Months Ended June 30, 2006</b>		<b>Nine Months Ended June 30, 2006</b>	
	<b>Gross</b>	<b>Net of tax</b>	<b>Gross</b>	<b>Net of tax</b>
Education services and facilities	\$ 127	\$ 77	\$ 352	\$ 214
Selling, general and administrative	987	601	2,867	1,746
Total stock-based compensation expense	\$ 1,114	\$ 678	\$ 3,219	\$ 1,960

As of June 30, 2006, unrecognized stock compensation expense related to unvested stock options and restricted stock awards was \$14.8 million, which is expected to be recognized over a weighted average period of 2.7 years.

**5. Weighted Average Number of Common Shares Outstanding**

Basic net income per share is calculated by dividing net income by the weighted average number of common shares outstanding for the period. Diluted net income per share reflects the assumed conversion of all dilutive securities. For the three and nine months ended June 30, 2006, approximately 654,000 shares and 605,000 shares, respectively, that could be issued under outstanding options, were not included in the determination of our diluted shares outstanding, as they were anti-dilutive. For the three and nine months ended June 30, 2005, approximately 564,000 shares and 294,000 shares, respectively, that could be issued under outstanding options, were not included in the determination of our diluted shares outstanding, as they were anti-dilutive.

The table below reflects the calculation of the weighted average number of common shares outstanding used in computing basic and diluted net income per common share:

	<b>Three Months Ended June 30,</b>		<b>Nine Months Ended June 30,</b>	
	<b>2005</b>	<b>2006</b>	<b>2005</b>	<b>2006</b>
Basic common shares outstanding	27,934	27,949	27,875	28,002
Dilutive effect of options related to the purchase of common stock	611	372	655	489
Diluted common shares outstanding	28,545	28,321	28,530	28,491

On February 28, 2006, our Board of Directors authorized the repurchase of up to \$30 million of our common stock in open market or privately negotiated transactions. The timing and actual number of shares purchased will depend on a variety of factors such as price, corporate and regulatory requirements and other prevailing market conditions. We may terminate or limit the stock repurchase program at any time without prior notice. At June 30, 2006, we have repurchased approximately 612,000 shares at a total cost of \$15.0 million.

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**UNIVERSAL TECHNICAL INSTITUTE, INC.**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**  
(In thousands, except per share amounts)

**6. Restricted Investments**

Restricted investments represent collateral provided to the issuer of our letter of credit in favor of the United States Department of Education (ED). At September 30, 2005, we had an outstanding letter of credit in favor of ED in the amount of \$14.4 million which was collateralized by a United States government agency discount note with a scheduled maturity in November 2005. During October 2005, we received notification from ED that we were no longer required to post a letter of credit, based upon ED's review of our 2004 fiscal year financial statements. ED returned the letter of credit in November 2005, and the restricted investment balance of \$16.2 million was released and became available for general corporate use.

**7. Property and Equipment**

Property and equipment, net consist of the following:

	<b>September 30, 2005</b>	<b>June 30, 2006</b>
Land	\$ 3,832	\$ 3,832
Building and building improvements	8,847	21,016
Leasehold improvements	17,720	38,496
Training equipment	33,823	43,686
Office and computer equipment	21,120	24,269
Curriculum development	1,326	1,312
Internally developed software	2,555	3,235
Vehicles	693	747
Construction in progress	14,575	10,945
	104,491	147,538
Less accumulated depreciation and amortization	(30,074)	(39,911)
	\$ 74,417	\$ 107,627

At September 30, 2005, construction in progress includes \$11.1 million of building improvements related to the retrofitting of our Norwood, Massachusetts building for our automotive program which was completed and placed in service during November 2005. At June 30, 2006, construction in progress includes \$3.7 million related to construction of our new Sacramento, California campus building and \$3.1 million related to our automotive program campus expansion in Orlando, Florida. The Orlando, Florida automotive program campus expansion is being completed in accordance with the terms of our lease agreement. We have recorded the aggregate construction costs incurred under the lease as a construction liability on our Balance Sheet at June 30, 2006.

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**UNIVERSAL TECHNICAL INSTITUTE, INC.**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**  
(In thousands, except per share amounts)

**8. Accounts Payable and Accrued Expenses**

Accounts payable and accrued expenses consist of the following:

	<b>September 30, 2005</b>	<b>June 30, 2006</b>
Accounts payable	\$ 9,765	\$ 9,432
Accrued compensation and benefits	21,073	20,829
Other accrued expenses	8,292	10,574
	<b>\$ 39,130</b>	<b>\$ 40,835</b>

**9. Revolving Credit Facility**

On July 5, 2006 we entered into a modification agreement of our credit agreement dated October 26, 2004 which provided a revolving line of credit in the amount of \$30.0 million and a standby letter of credit facility in the amount of \$20.0 million. The modification agreement eliminated the standby letter of credit facility, of which \$0 was outstanding at the date of the modification and changed the minimum quarterly current ratio financial covenant as follows: 0.50 to 1.00 through June 30, 2007 and 0.60 to 1.00 on September 30, 2007 and thereafter. Prior to the modification, the minimum quarterly current ratio financial covenant was 0.60 to 1.00 at September 30, 2006 and thereafter. The revolving line of credit is unsecured and guaranteed by our wholly owned subsidiary UTI Holdings, Inc. and each of its wholly owned subsidiaries.

At June 30, 2006, we have no borrowings under our credit facility and we were in compliance with all covenants.

**10. Commitments and Contingencies*****Legal***

In the ordinary conduct of our business, we are periodically subject to lawsuits, investigations and claims, including, but not limited to, claims involving students or graduates and routine employment matters. Although we cannot predict with certainty the ultimate resolution of lawsuits, investigations and claims asserted against us, we do not believe that any currently pending legal proceeding to which we are a party will have a material adverse effect on our business, results of operations, cash flows or financial condition.

As we have previously reported, in April 2004, we received a letter on behalf of nine former employees of National Technology Transfer, Inc. (NTT), an entity that we purchased in 1998 and subsequently sold, making a demand for an aggregate payment of approximately \$0.3 million and 19,756 shares of our common stock. On February 23, 2005, the former employees filed suit in Maricopa County, Arizona Superior Court. We filed a motion for summary judgment and by minute entry dated December 22, 2005, the Arizona Superior Court granted our motion on all claims. The plaintiffs filed a motion requesting that the court amend and vacate its minute entry. The Court denied plaintiffs motion on March 30, 2006. On May 1, 2006, the Court entered final judgment in our favor and against plaintiffs on all claims. Plaintiffs filed a notice of appeal on May 22, 2006 and the matter is currently pending before the Arizona Court of Appeals.

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**UNIVERSAL TECHNICAL INSTITUTE, INC.**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**  
(In thousands, except per share amounts)

**11. Segment Reporting**

We follow SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information. SFAS No. 131 establishes standards for the way that public business enterprises report certain information about operating segments in their financial reports. Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated on a regular basis by the chief operating decision maker, or decision-making group, in assessing performance of the segment and in deciding how to allocate resources to an individual segment. SFAS No. 131 also established standards for related disclosures about products and services, geographic areas and major customers.

Our principal business is providing post-secondary education. We also provide manufacturer-specific training, and these operations are managed separately from our campus operations. These operations do not currently meet the quantitative criteria for segments and therefore are not deemed reportable under SFAS No. 131 and are reflected in the Other category. Corporate expenses are allocated to Post-Secondary Education and the Other category.

	<b>Three Months Ended June 30, 2005</b>			<b>Three Months Ended June 30, 2006</b>		
	<b>Post- Secondary Education</b>	<b>Other</b>	<b>Total</b>	<b>Post- Secondary Education</b>	<b>Other</b>	<b>Total</b>
Net revenues	\$ 71,885	\$4,189	\$ 76,074	\$ 80,081	\$4,053	\$ 84,134
Operating income (loss)	\$ 11,089	\$ 361	\$ 11,450	\$ 5,784	\$ (73)	\$ 5,711
Depreciation and amortization	\$ 2,413	\$ 113	\$ 2,526	\$ 3,461	\$ 102	\$ 3,563
Goodwill	\$ 20,579	\$	\$ 20,579	\$ 20,579	\$	\$ 20,579
Assets	\$168,958	\$3,140	\$172,098	\$211,087	\$3,317	\$214,404

	<b>Nine Months Ended June 30, 2005</b>			<b>Nine Months Ended June 30, 2006</b>		
	<b>Post- Secondary Education</b>	<b>Other</b>	<b>Total</b>	<b>Post- Secondary Education</b>	<b>Other</b>	<b>Total</b>
Net revenues	\$214,707	\$12,185	\$226,892	\$246,795	\$11,537	\$258,332
Operating income (loss)	\$ 40,486	\$ 869	\$ 41,355	\$ 34,692	\$ (207)	\$ 34,485
Depreciation and amortization	\$ 6,762	\$ 329	\$ 7,091	\$ 9,839	\$ 311	\$ 10,150
Goodwill	\$ 20,579	\$	\$ 20,579	\$ 20,579	\$	\$ 20,579
Assets	\$168,958	\$ 3,140	\$172,098	\$211,087	\$ 3,317	\$214,404

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**Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*The following discussion and analysis should be read in conjunction with the consolidated financial statements and related notes included in this report and those in our 2005 Annual Report on Form 10-K filed with the Securities and Exchange Commission on December 14, 2005. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from those anticipated in such forward-looking statements as a result of certain factors, including but not limited to, those described under Cautionary Factors That May Affect Future Results.*

**Critical Accounting Policies and Estimates**

Our critical accounting policies are disclosed in our 2005 Annual Report on Form 10-K. During the three and nine months ended June 30, 2006, there have been no significant changes in our critical accounting policies, other than stock-based compensation discussed below.

**Stock-based compensation.** Effective October 1, 2005, we adopted SFAS No. 123 (R) Share-Based Payment using the modified prospective application transition method. Prior to adoption of SFAS No. 123(R), we accounted for stock-based awards to employees using the intrinsic value method in accordance with APB No. 25 as allowed under SFAS No. 123 Accounting for Stock-Based Compensation. Our consolidated financial statements for prior periods have not been restated to reflect, and do not include, the impact of SFAS No. 123(R). As of June 30, 2006, unrecognized stock compensation expense related to unvested stock options and restricted stock awards was \$14.8 million, which is expected to be recognized over a weighted average period of 2.7 years.

**Recent Accounting Pronouncements**

For information regarding recent accounting pronouncements, see Note 3 to our unaudited condensed consolidated financial statements within Part I, Item 1 of this report.

**Overview**

Our net revenues for the third quarter were \$84.1 million, an increase of 10.6% from the prior year and our net income for the third quarter was \$4.5 million, a decrease of 40.9% from the prior year. Our decrease in net income is due to lower capacity utilization in conjunction with higher compensation and related costs, sales and marketing costs, depreciation and the recognition of stock-based compensation expense under SFAS No. 123(R) of \$1.1 million.

Recruitment efforts and student starts lag the prior year due to a variety of factors. A strong labor market across the country coupled with affordability concerns associated with climbing interest rates and increased gas and housing prices have made it more challenging and expensive to recruit and start students. The transition to a new advertising agency and call center during the second quarter of our current fiscal year contributed to a disruption in lead flow. During our third quarter, lead flow has improved and we believe the improvement is associated with the completion of the transition of our advertising agency and call center vendor relationships as well as the development of new creative advertisements and promotional materials and additional spending in advertising.

Historically, we have been able to overcome such external forces by modifying educational programs, utilizing different pricing strategies and investing in sales and marketing. In response to both the external environment and internal operational issues, we have implemented a plan that focuses on stabilizing and improving key operating efforts. We are uncertain when we will realize the benefits of these efforts.



**Table of Contents****Results of Operations**

The following table sets forth selected statements of operations data as a percentage of net revenues for each of the periods indicated.

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2005	2006	2005	2006
Net Revenues	100.0%	100.0%	100.0%	100.0%
Operating expenses:				
Educational services and facilities	48.7%	53.2%	46.4%	49.5%
Selling, general and administrative	36.2%	40.0%	35.4%	37.2%
Total operating expenses	84.9%	93.2%	81.8%	86.7%
Income from operations	15.1%	6.8%	18.2%	13.3%
Interest income	-0.5%	-1.0%	-0.4%	-0.9%
Income before income taxes	15.6%	7.8%	18.6%	14.2%
Income tax expense	5.6%	2.4%	6.9%	5.3%
Net income	10.0%	5.4%	11.7%	8.9%

**Three Months Ended June 30, 2006 Compared to Three Months Ended June 30, 2005 and Nine Months Ended June 30, 2006 Compared to Nine Months Ended June 30, 2005**

**Net revenues.** Our revenues for the three months ended June 30, 2006 were \$84.1 million, representing an increase of \$8.1 million, or 10.6%, as compared to net revenues of \$76.1 million for the three months ended June 30, 2005. This increase was due to tuition increases of approximately 6.0% and a 4.1% increase in the average undergraduate full-time student enrollment during the three months ended June 30, 2006. Average undergraduate full-time student enrollment increased to 15,166 for the three months ended June 30, 2006 as compared to 14,572 for the three months ended June 30, 2005.

Our revenues for the nine months ended June 30, 2006 were \$258.3 million, representing an increase of \$31.4 million, or 13.9%, as compared to net revenues of \$226.9 million for the nine months ended June 30, 2005. This increase was due to a 7.7% increase in the average undergraduate full-time student enrollment and tuition increases of approximately 5.7%. Average undergraduate full-time student enrollment increased to 16,324 for the nine months ended June 30, 2006 as compared to 15,155 for the nine months ended June 30, 2005.

**Educational services and facilities expenses.** Our educational services and facilities expenses for the three months ended June 30, 2006 were \$44.8 million, an increase of \$7.7 million, as compared to educational services and facilities expenses of \$37.1 million for the three months ended June 30, 2005. Our educational services and facilities expenses for the nine months ended June 30, 2006 were \$127.9 million, an increase of \$22.5 million, as compared to educational services and facilities expenses of \$105.3 million for the nine months ended June 30, 2005. The increases in these expenses for the three and nine months ended June 30, 2006 are primarily related to increases in compensation and related costs of approximately \$4.4 million and \$13.3 million, respectively, attributable to the staffing of education management, instructors and student support functions related to our expansion efforts as well as additional staffing to accommodate current and future growth. Recent

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expansion activities also increased operating costs, as compared to the comparable periods in the previous year. Campus rent and utilities and depreciation expense increased approximately \$0.8 million and \$0.9 million, respectively, for the third quarter ended June 30, 2006 and increased approximately \$2.3 million and \$2.7 million, respectively, for the nine months ended June 30, 2006. In addition, we recognized stock compensation expense of approximately \$0.1 million in the third quarter ended June 30, 2006 and \$0.4 million for the nine months ended June 30, 2006 as a result of our adoption of SFAS No. 123(R). We did not recognize any stock compensation expense as a component of educational services and facilities in the previous comparative periods.

Educational services and facilities expenses as a percentage of net revenues increased to 53.2% for the three months ended June 30, 2006 as compared to 48.7% for the three months ended June 30, 2005. Educational services and facilities expenses as a percentage of net revenues increased to 49.5% for the nine months ended June 30, 2006 as compared to 46.4% for the nine months ended June 30, 2005. The increase in educational services and facilities expenses as a percentage of net revenues for the three months and nine months ended June 30, 2006 is attributable to decreased capacity utilization.

We begin to incur educational services and facilities costs associated with instructor compensation and occupancy costs during the 12 to 15 months in advance of new campus openings. The majority of our start-up costs are incurred in the nine month period prior to a campus opening. For the three months ended June 30, 2006, start-up costs were \$2.9 million related to our Norwood, Massachusetts campus and \$1.8 million related to our Sacramento, California campus for total start-up costs of approximately \$4.7 million. For the three months ended June 30, 2005, start-up costs were \$0.8 million related to our Norwood, Massachusetts campus. For the nine months ended June 30, 2006, start-up costs were \$6.9 million related to our Norwood, Massachusetts campus and \$4.1 million related to our Sacramento, California campus for total start-up costs of approximately \$11.0 million. For the nine months ended June 30, 2005 start-up costs were \$1.1 million related to our Norwood, Massachusetts campus.

***Selling, general and administrative expenses.*** Our selling, general and administrative expenses for the three months ended June 30, 2006 were \$33.6 million, an increase of \$6.1 million, as compared to selling, general and administrative expenses of \$27.6 million for the three months ended June 30, 2005. Our selling, general and administrative expenses for the nine months ended June 30, 2006 were \$96.0 million, an increase of \$15.8 million, as compared to selling, general and administrative expenses of \$80.2 million for the nine months ended June 30, 2005. The increases in these expenses for the three and nine months ended June 30, 2006 are related to increases in compensation and related costs of approximately \$2.0 million and \$6.4 million, respectively, primarily due to increased personnel associated with sales and marketing activities and other organizational support. In addition, we recognized stock compensation expense of approximately \$1.0 million and \$2.8 million for the three and nine months ending June 30, 2006, respectively, attributable to our adoption of SFAS No. 123(R). Selling, general and administrative expenses were also impacted by increases in advertising expense of approximately \$1.4 million and \$3.0 million, for the three and nine months ended June 30, 2006, respectively, due to increased advertising to support new applicants and increased contract services of approximately \$0.7 million for both the three and nine months ended June 30, 2006 primarily due to \$0.5 million in costs incurred associated with the termination of new campus site selection activities. These increases were partially offset by a decrease for the three and nine months ended June 30, 2006 in professional services of approximately \$0.1 million and \$0.7 million, respectively, primarily attributable to reduced legal costs and lower costs associated with Sarbanes-Oxley compliance efforts.

Selling, general and administrative expenses as a percentage of net revenues increased to 40.0% for the three months ended June 30, 2006 as compared to 36.2% for the three months ended June 30, 2005. Selling, general and administrative expenses as a percentage of net revenues increased to 37.2% for the nine months ended June 30, 2006 as compared to 35.4% for the nine months ended June 30, 2005. The increase in selling, general and administrative expenses as a percentage of net revenues for the three and nine months ended June 30, 2006 is

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due to stock-based compensation expense attributable to our adoption of SFAS No. 123(R) and additional spending in advertising.

We begin to incur selling, general and administrative expenses associated with campus administration and sales force compensation and advertising costs during the 12 to 15 months in advance of new campus openings. The majority of our start-up costs are incurred in the nine-month period prior to a campus opening. For the three months ended June 30, 2006, start-up costs were \$1.5 million related to our Norwood, Massachusetts campus and \$1.3 million related to our Sacramento, California campus for total start-up costs of approximately \$2.8 million. For the three months ended June 30, 2005, start-up costs were \$1.2 million related to our Norwood, Massachusetts campus and \$0.4 million related to our Sacramento, California campus for total start-up costs of \$1.6 million. For the nine months ended June 30, 2006, start-up costs were \$4.3 million related to our Norwood, Massachusetts campus and \$3.5 million related to our Sacramento, California campus for total start-up costs of approximately \$7.8 million. For the nine months ended June 30, 2005 start-up costs were \$2.0 million related to our Norwood, Massachusetts campus and \$0.6 million related to our Sacramento, California campus for total start-up costs of \$2.6 million.

**Interest income.** Our interest income for the three months ended June 30, 2006 was approximately \$0.8 million, representing an increase of approximately \$0.4 million compared to interest income of approximately \$0.4 million for the three months ended June 30, 2005. Our interest income for the nine months ended June 30, 2006 was approximately \$2.4 million, representing an increase of approximately \$1.4 million compared to interest income of approximately \$1.0 million for the nine months ended June 30, 2005. The increase in interest income is primarily attributable to the increase in available investment funds as well as higher interest rate returns.

**Income taxes.** Our provision for income taxes for the three months ended June 30, 2006 was approximately \$2.0 million, or 31.0% of pretax income, compared to approximately \$4.2 million, or 35.8% of pretax income for the three months ended June 30, 2005. Our provision for income taxes for the nine months ended June 30, 2006 was approximately \$13.8 million, or 37.4% of pretax income, compared to approximately \$15.7 million, or 37.1% of pretax income for the nine months ended June 30, 2005. The higher effective rate for the nine months ended June 30, 2006 as compared to the nine months ended June 30, 2005 was primarily attributable to higher statutory state tax rates and the reduction of state tax incentives partially offset by the release of tax reserves due to the closure of additional tax years subject to audit. In addition, in the third quarter of 2006, we recognized approximately \$0.8 million as additional paid in capital in connection with the release of tax reserves.

**Liquidity and Capital Resources**

We finance our operating activities and our internal growth through cash generated from operations. Our net cash from operations was \$28.8 million for the nine months ended June 30, 2006 compared to \$52.3 million for the nine months ended June 30, 2005. Cash provided by operations for the nine month period ended June 30, 2005 includes the favorable impact of the release of restricted cash in the amount of \$10.4 million.

A majority of our revenues are derived from Title IV Programs. Federal regulations dictate the timing of disbursements of funds under Title IV Programs. Students must apply for a new loan for each academic year (thirty-week periods) and loan funds are generally provided by lenders in two disbursements for each academic year. The first disbursement is usually received 30 days after the start of a student's academic year and the second disbursement is typically received at the beginning of the sixteenth week from the start of the student's academic year. Certain types of grants and other funding are not subject to a 30-day delay. Our undergraduate programs are typically designed to be completed in 12 to 18 months. These timing factors, together with the timing of when our students begin their programs, affect our operating cash flow.

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For the nine months ended June 30, 2006, our cash flows provided by operating activities were \$28.8 million due to net income of \$23.0 million, plus net adjustments of \$14.7 million for non-cash and other items less \$8.9 million related to the change in our operating assets and liabilities.

For the nine months ended June 30, 2005, our cash flows provided by operating activities were \$52.3 million due to net income of \$26.6 million, plus net adjustments of \$10.5 million for non-cash and other items plus \$15.2 million related to the change in our operating assets and liabilities.

***Changes in non-cash items***

For the nine months ended June 30, 2006, the primary adjustments to our net income for non-cash and other items were depreciation and amortization of \$10.2 million, substantially all of which was depreciation, bad debt expense of \$3.8 million and stock-based compensation of \$3.4 million primarily related to our adoption of SFAS No. 123(R) partially offset by a reduction in deferred income taxes of \$1.8 million and our excess tax benefits from stock-based compensation of \$1.0 million.

For the nine months ended June 30, 2005, the primary adjustments to our net income for non-cash and other items were depreciation and amortization of \$7.1 million, substantially all of which was depreciation, bad debt expense of \$3.0 million, tax benefit derived from option exercises of \$1.1 million and stock-based compensation of \$0.3 million partially offset by a reduction in deferred income taxes of \$1.1 million.

***Changes in operating assets and liabilities***

For the nine months ended June 30, 2006, the cash outflows of \$8.9 million relating to changes in our operating assets and liabilities was primarily due to changes in accounts receivables, deferred revenue, accounts payable and accrued expenses, income tax payable and prepaid expenses. The timing of tuition funding resulted in a decrease in accounts receivable of \$4.8 million and a decrease in deferred revenue of \$3.4 million resulting in a net cash inflow of \$1.4 million. The cash used in accounts payable and accrued expenses primarily related to payments related to performance bonuses of approximately \$4.0 million and a bank overdraft of \$4.2 million partially offset by approximately \$1.0 million related to the timing and fluctuation of the accounts payable cycle. The bank overdraft is attributable to a treasury management process whereby we are able to maximize our invested cash while providing cash to our primary bank to cover individual daily requirements. The decrease in income taxes of \$1.8 million was attributable to the payment of estimated taxes. The increase in prepaid expenses of \$1.1 million was primarily related to the timing of payment for advertising costs. Other adjustments provided net cash outflow of \$0.2 million.

For the nine months ended June 30, 2005, the \$15.2 million relating to the change in our operating assets and liabilities was primarily due to changes in restricted cash and prepaid expenses. A significant non-recurring benefit in operating assets and liabilities was the release of \$10.4 million in restricted cash related to collateral provided for a letter of credit issued in favor of ED. The collateral was released upon expiration of the letter of credit. The increase in prepaid expenses of \$3.2 million was primarily attributable to the timing of payment for facility rents and other services.

Our days sales outstanding (DSO) in accounts receivable was approximately 18 days at June 30, 2006 compared to approximately 21 days at June 30, 2005. DSO is impacted by the timing of Title IV tuition funding as well as our total student population.

At June 30, 2006, we had a working capital deficit of approximately \$0.1 million primarily attributable to the use of \$15.0 million in cash used to repurchase stock in accordance with our stock repurchase program.

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***Investing Activities***

For the nine months ended June 30, 2006, cash flows used in investing activities were \$18.8 million and were primarily related to the purchase of \$35.1 million in capital expenditures primarily associated with new campus construction and existing campus expansions partially offset by proceeds of \$16.3 million from the release of our restricted investments that provided cash collateral for our letter of credit issued in favor of ED.

For the nine months ended June 30, 2005, cash flows used in investing activities were \$49.8 million and were primarily related to the purchase of \$34.2 million in capital expenditures and our net investment of approximately \$15.8 million used to purchase securities.

***Financing Activities***

For the nine months ended June 30, 2006, cash flows used in financing activities were \$7.2 million and were primarily due to proceeds of \$2.6 million related to stock issued under employee option plans, a bank overdraft of \$4.2 million resulting from the timing of payments issued through controlled disbursement accounts and \$1.0 million related to recognition of the excess tax benefit from stock-based compensation in connection with our adoption of SFAS No. 123 (R) partially offset by \$15.0 million used for the repurchase of our stock.

For the nine months ended June 30, 2005, cash flows from financing activities were \$2.2 million and were primarily due to proceeds of \$2.4 million related to stock issued under employee option plans partially offset by \$0.2 million in a distribution to participating shareholders related to the sale of land held for sale.

On February 28, 2006 our Board of Directors authorized the repurchase of up to \$30 million of our common stock in open market or privately negotiated transactions. The timing and actual number of shares purchased will depend on a variety of factors such as price, corporate and regulatory requirements and other prevailing market conditions. We may terminate or limit the stock repurchase program at any time without prior notice. At June 30, 2006, we have repurchased approximately 612,000 shares at a total cost of \$15.0 million.

***Future Liquidity Sources***

Based on past performance and current expectations, we believe that our cash flows from operations will satisfy our working capital needs, capital expenditures, commitments, and other liquidity requirements associated with our operations through the next 12 months. We believe that the most strategic uses of our cash resources include expanding new and existing campuses, expanding our program offerings, marketing to increase capacity utilization and repurchasing our stock. In addition, our long term strategy includes considering strategic acquisitions. To the extent that potential acquisitions are large enough to require financing beyond cash from operations and available borrowings under our credit facility, we may incur additional debt or issue debt resulting in increased interest expense.

***Credit Facility***

During fiscal 2005, under the terms of our credit agreement, we issued a letter of credit in favor of ED in the amount of \$14.4 million that was collateralized by a \$16.2 million restricted investment held in marketable securities. During October 2005, we were notified by ED that our letter of credit was no longer required. Upon release of the letter of credit, our restricted investment balance of approximately \$16.2 million became available for general corporate use.

On July 5, 2006 we entered into a modification agreement of our credit agreement dated October 26, 2004 which provided a revolving line of credit in the amount of \$30.0 million and a standby letter of credit facility in

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the amount of \$20.0 million. The modification agreement eliminated the standby letter of credit facility, of which \$0 was outstanding at the date of the modification and changed the minimum quarterly current ratio financial covenant as follows: 0.50 to 1.00 through June 30, 2007 and 0.60 to 1.00 on September 30, 2007 and thereafter. Prior to the modification, the minimum quarterly current ratio financial covenant was 0.60 to 1.00 at September 30, 2006 and thereafter. The revolving line of credit is unsecured and guaranteed by our wholly owned subsidiary UTI Holdings, Inc. and each of its wholly owned subsidiaries.

At June 30, 2006, we have no borrowings under our credit facility and we were in compliance with all covenants.

**Seasonality and Trends**

Our net revenues and operating results normally fluctuate as a result of seasonal variations in our business, principally due to changes in total student population. Student population varies as a result of new student enrollments, graduations and student attrition. Historically, our schools have had lower student populations in our third fiscal quarter, which ends on June 30, than in the remainder of our fiscal year because fewer students are enrolled during the summer months. In addition, school is not in session during the one-week holiday break which occurs in December. As a result, first quarter revenue does not correlate to the peak in student population. Our normal operating expenses, however, do not vary significantly with changes in our student population and net revenues and, as a result, such expenses do not fluctuate significantly on a quarterly basis. We expect quarterly fluctuation in operating results to continue as a result of seasonal enrollment patterns. Such patterns may change however, as a result of new school openings, new program introductions, increased enrollments of adult students, increased investment in sales and marketing or acquisitions.

Operating income is negatively impacted during the initial start up of new campus openings. We incur sales and marketing costs as well as campus personnel costs in advance of the campus opening. Typically we begin to incur such costs approximately 12 to 15 months in advance of the campus opening with the majority of the costs being incurred in the nine-month period prior to a campus opening. We incurred start-up losses of approximately \$6.6 million during the nine months ended June 30, 2006 related to our Norwood, Massachusetts and Sacramento, California campuses, compared to start-up losses of approximately \$3.4 million during the nine months ended June 30, 2005 related to our Norwood, Massachusetts and Sacramento, California campuses. Our Norwood campus opened in June 2005 and our Sacramento campus opened at its temporary location in October 2005, moving to its permanent location in June 2006.

**Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Our principal exposure to market risk relates to interest rate changes. As of June 30, 2006, we do not have any term debt. Consequently, we have minimal financial exposure to market risk.

**Cautionary Factors That May Affect Future Results**

This report contains forward-looking information about our financial results, estimates and our business prospects that involve substantial risks and uncertainties. From time to time, we also may provide oral or written forward-looking statements in other materials we release to the public. Forward-looking statements are expressions of our current expectations or forecasts of future events. You can identify these statements by the fact that they do not relate strictly to historic or current facts. They often include words such as anticipate, estimate, expect, project, in plan, believe, will, and other words and terms of similar meaning in connection with any discussion of future operating or financial performance. In particular, these include statements relating to future actions, future performance or results, expenses, the outcome of contingencies, such as legal proceedings, and financial results. Among the factors that could cause actual results to differ materially are the following:

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our ability to maintain or renew any required regulatory approvals, standards, accreditation or state authorization;

possible failure or inability to obtain regulatory consents and certifications for new campuses and campus expansions;

changes in laws and regulations affecting post-secondary education, including Title IV funding;

governmental inquiries, compliance reviews or investigations and the potential for increased litigation;

regulatory investigations of, or actions commenced against, other companies in our industry;

our ability to manage our planned growth, both internally and at new or existing campuses;

competitive developments affecting our industry, including pricing pressures in newer markets;

our ability to maintain and expand existing industry relationships;

our ability to recruit and retain key personnel;

changes in demand for our programs;

increased investment in management and capital resources;

increases in interest rates or state budget constraints adversely affecting a student's ability to secure additional loans;

lower rates of unemployment;

the timing and number of new campuses that we open or acquire;

growth in costs and expenses;

construction delays with respect to new or expanding campuses;

economic slowdown that affects any significant portion of our customer base, including economic slowdown in areas of limited geographic scope if markets in which we have significant operations are impacted by such slowdown;

the effectiveness of our advertising and promotional efforts;

changes in generally accepted accounting principles;

our ability to maintain compliance with Section 404 of Sarbanes-Oxley;

any changes in business, political and economic conditions due to the threat of future terrorist activity in the U.S. and other parts of the world, and related U.S. military action overseas; and

potential increased competition.

We cannot guarantee any forward-looking statement will be realized, although we believe we have been prudent in our plans and assumptions. Achievement of future results is subject to risks, uncertainties and inaccurate assumptions. Should known or unknown risks or uncertainties materialize, or should underlying assumptions prove inaccurate, actual results could vary materially from past results and those anticipated, estimated or projected. Investors should bear this in mind as they consider forward-looking statements.

We undertake no obligation to publicly update forward-looking statements, whether as a result of new information, future events or otherwise. You are advised, however, to consult any further disclosures we make on related subjects in our Form 10-Q, 8-K and 10-K reports to the Securities and Exchange Commission. The Form 10-K that we filed with the SEC on December 14, 2005 listed various important factors that could cause actual results to differ materially from expected and historic results. We note these factors for investors as permitted by the Private Securities Litigation Reform Act of 1995. Readers can find them under the heading **Cautionary Factors That May Affect Future Results** in the Form 10-K. We incorporate that section of the Form 10-K in this filing and investors should refer to it. You should understand that it is not possible to predict or identify all such factors. Consequently, you should not consider any such list to be a complete set of all potential risks or uncertainties. Our filings with the SEC may be accessed at the SEC's website at [www.sec.gov](http://www.sec.gov).



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**Item 4. CONTROLS AND PROCEDURES**

**Disclosure Controls and Procedures**

Under the supervision and with the participation of our management, including the Chief Executive Officer and Chief Financial Officer, we have evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act), pursuant to Exchange Act Rule 13a-15 as of the end of the period covered by this report. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective in ensuring that (i) information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms and (ii) information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the Company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

**Changes in Internal Control Over Financial Reporting**

There were no changes in our internal control over financial reporting identified in connection with the evaluation required by Exchange Act Rule 13a-15(d) that occurred during the quarter ended June 30, 2006 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**Table of Contents****PART II. OTHER INFORMATION****Item 1. LEGAL PROCEEDINGS**

In the ordinary conduct of our business, we are periodically subject to lawsuits, investigations and claims, including, but not limited to, claims involving students or graduates and routine employment matters. Although we cannot predict with certainty the ultimate resolution of lawsuits, investigations and claims asserted against us, we do not believe that any currently pending legal proceeding to which we are a party will have a material adverse effect on our business, results of operations, cash flows or financial condition.

As we have previously reported, in April 2004, we received a letter on behalf of nine former employees of National Technology Transfer, Inc. (NTT), an entity that we purchased in 1998 and subsequently sold, making a demand for an aggregate payment of approximately \$0.3 million and 19,756 shares of our common stock. On February 23, 2005, the former employees filed suit in Maricopa County, Arizona Superior Court. We filed a motion for summary judgment and by minute entry dated December 22, 2005, the Arizona Superior Court granted our motion on all claims. The plaintiffs filed a motion requesting that the court amend and vacate its minute entry. The Court denied plaintiffs motion on March 30, 2006. On May 1, 2006, the Court entered final judgment in our favor and against plaintiffs on all claims. Plaintiffs filed a notice of appeal on May 22, 2006 and the matter is currently pending before the Arizona Court of Appeals.

**Item 1A. RISK FACTORS**

Information regarding risk factors appears in Part I, Item 3 of this report under the heading **Cautionary Factors That May Affect Future Results** and in Part I, Item 1 of our 2005 Annual Report on Form 10-K filed with the Securities and Exchange Commission on December 14, 2005.

**Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

The following table summarizes the purchase of equity securities made through our stock repurchase program:

**ISSUER PURCHASES OF EQUITY SECURITIES**

<b>Period</b>	<b>(a) Total Number of Shares Purchased</b>	<b>(b) Average Price Paid per Share</b>	<b>(c) Total Number of Shares Purchased as Part of Publicly Announced Plans</b>	<b>(d) Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans Or Programs</b>
May 12, 2006 - May 31, 2006	302,900	\$ 25.09	302,900	\$22.4 million
June 1, 2006 - June 15, 2006	308,750	\$ 23.98	308,750	\$15.0 million
Total	611,650	\$ 24.53	611,650	\$15.0 million

(1) Our stock repurchase program was announced on

March 6, 2006.  
All shares were  
repurchased  
pursuant to this  
program.

- (2) On February 28,  
2006, the Board  
of Directors  
authorized the  
repurchase of up  
to \$30.0 million  
of our  
outstanding  
common stock  
in open market  
or privately  
negotiated  
transactions.

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- (3) Our stock repurchase program has no expiration date, however, we may terminate or limit the stock repurchase program at any time without prior notice.

**Item 6. EXHIBITS**

(a) Exhibits (filed herewith):

<b>Number</b>	<b>Description</b>
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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**SIGNATURES**

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

UNIVERSAL TECHNICAL INSTITUTE,  
INC.

Dated: August 9, 2006

By: /s/ Jennifer L. Haslip  
Jennifer L. Haslip  
Senior Vice President, Chief Financial  
Officer,  
Treasurer and Assistant Secretary  
(Principal Financial Officer and Duly  
Authorized Officer)

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**INDEX TO EXHIBITS**

<b>Number</b>	<b>Description</b>
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