

CREDIT ACCEPTANCE CORP  
Form 10-Q  
May 02, 2011

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2011

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 000-20202  
CREDIT ACCEPTANCE CORPORATION  
(Exact name of registrant as specified in its charter)

MICHIGAN  
(State or other jurisdiction of incorporation or  
organization)

38-1999511  
(I.R.S. Employer Identification No.)

25505 WEST TWELVE MILE ROAD  
SOUTHFIELD, MICHIGAN  
(Address of principal executive offices)

48034-8339  
(Zip Code)

Registrant's telephone number, including area code: 248-353-2700

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 whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting  
company   
(Do not check if a smaller reporting company)

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

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

The number of shares of Common Stock, par value \$0.01, outstanding on April 22, 2011 was 25,591,344.

---

TABLE OF CONTENTS

PART I. — FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

Consolidated Statements of Income – Three months ended  
March 31, 2011 and 2010 1

Consolidated Balance Sheets – As of March 31, 2011 and  
December 31, 2010 2

Consolidated Statements of Cash Flows – Three months ended  
March 31, 2011 and 2010 3

Notes to Consolidated Financial Statements 4

ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS  
OF FINANCIAL CONDITION AND RESULTS OF  
OPERATIONS 23

ITEM 3. QUANTITATIVE AND QUALITATIVE  
DISCLOSURES ABOUT MARKET RISK 33

ITEM 4. CONTROLS AND PROCEDURES 33

PART II. — OTHER INFORMATION

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES  
AND USE OF PROCEEDS 34

ITEM 6. EXHIBITS 34

SIGNATURE 35

INDEX OF EXHIBITS 36

EX-31.A  
EX-31.B  
EX-32.A  
EX-32.B

## PART I. - FINANCIAL INFORMATION

## ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

CREDIT ACCEPTANCE CORPORATION  
CONSOLIDATED STATEMENTS OF INCOME  
(UNAUDITED)

| (In thousands, except per share data)                               | For the Three Months<br>Ended March 31, |           |
|---|---|-----------|
|   | 2011                                    | 2010      |
| Revenue:  |   |           |
| Finance charges   | \$ 106,503                              | \$ 89,663 |
| Premiums earned   | 8,543                                   | 7,704     |
| Other income  | 8,466                                   | 5,895     |
| Total revenue   | 123,512                                 | 103,262   |
| Costs and expenses:   |   |           |
| Salaries and wages  | 16,071                                  | 16,110    |
| General and administrative  | 5,633                                   | 6,542     |
| Sales and marketing   | 6,409                                   | 4,810     |
| Provision for credit losses   | 8,916                                   | 6,426     |
| Interest  | 12,623                                  | 11,705    |
| Provision for claims  | 6,599                                   | 5,212     |
| Total costs and expenses  | 56,251                                  | 50,805    |
| Income from continuing operations before provision for income taxes | 67,261                                  | 52,457    |
| Provision for income taxes  | 24,070                                  | 20,442    |
| Income from continuing operations                                   | 43,191                                  | 32,015    |
| Discontinued operations   |   |           |
| Loss from discontinued United Kingdom operations                    | -                                       | (5)       |
| Provision for income taxes  | -                                       | -         |
| Loss from discontinued operations                                   | -                                       | (5)       |
| Net income  | \$ 43,191                               | \$ 32,010 |
| Net income per share:   |   |           |
| Basic   | \$ 1.59                                 | \$ 1.03   |
| Diluted   | \$ 1.57                                 | \$ 1.01   |
| Income from continuing operations per share:                        |   |           |
| Basic   | \$ 1.59                                 | \$ 1.03   |
| Diluted   | \$ 1.57                                 | \$ 1.01   |
| Loss from discontinued operations per share:                        |   |           |
| Basic   | \$ -                                    | \$ -      |
| Diluted   | \$ -                                    | \$ -      |
| Weighted average shares outstanding:                                |   |           |
| Basic   | 27,196                                  | 31,042    |
| Diluted   | 27,489                                  | 31,584    |

See accompanying notes to consolidated financial statements.

CREDIT ACCEPTANCE CORPORATION  
CONSOLIDATED BALANCE SHEETS

(In thousands, except per share data)

|   | As of                            |                      |
|---|----------------------------------|----------------------|
|   | March 31,<br>2011<br>(Unaudited) | December<br>31, 2010 |
| <b>ASSETS:</b>  |                                  |                      |
| Cash and cash equivalents   | \$ 4,585                         | \$ 3,792             |
| Restricted cash and cash equivalents  | 81,370                           | 66,536               |
| Restricted securities available for sale  | 806                              | 805                  |
| Loans receivable (including \$7,506 and \$9,031 from affiliates as of March 31, 2011 and December 31, 2010, respectively)   | 1,488,356                        | 1,344,881            |
| Allowance for credit losses   | (135,868)                        | (126,868)            |
| Loans receivable, net   | 1,352,488                        | 1,218,013            |
| Property and equipment, net   | 16,864                           | 16,311               |
| Income taxes receivable   | 708                              | 12,002               |
| Other assets  | 35,269                           | 26,056               |
| <b>Total Assets</b>   | <b>\$ 1,492,090</b>              | <b>\$ 1,343,515</b>  |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY:</b>  |                                  |                      |
| <b>Liabilities:</b>   |                                  |                      |
| Accounts payable and accrued liabilities  | \$ 97,194                        | \$ 75,297            |
| Revolving secured line of credit  | 132,800                          | 136,700              |
| Secured financing   | 398,600                          | 300,100              |
| Mortgage note   | 4,465                            | 4,523                |
| Senior notes  | 350,455                          | 244,344              |
| Deferred income taxes, net  | 102,724                          | 108,077              |
| Income taxes payable  | 10,542                           | -                    |
| <b>Total Liabilities</b>  | <b>1,096,780</b>                 | <b>869,041</b>       |
| <b>Commitments and Contingencies - See Note 12</b>  |                                  |                      |
| <b>Shareholders' Equity:</b>  |                                  |                      |
| Preferred stock, \$.01 par value, 1,000 shares authorized, none issued  | -                                | -                    |
| Common stock, \$.01 par value, 80,000 shares authorized, 25,584 and 27,304 shares issued and outstanding as of March 31, 2011 and December 31, 2010, respectively | 256                              | 273                  |
| Paid-in capital   | 34,878                           | 30,985               |
| Retained earnings   | 360,245                          | 443,326              |
| Accumulated other comprehensive loss, net of tax of \$40 and \$64 as of March 31, 2011 and December 31, 2010, respectively  | (69)                             | (110)                |
| <b>Total Shareholders' Equity</b>   | <b>395,310</b>                   | <b>474,474</b>       |
| <b>Total Liabilities and Shareholders' Equity</b>   | <b>\$ 1,492,090</b>              | <b>\$ 1,343,515</b>  |

See accompanying notes to consolidated financial statements.



CREDIT ACCEPTANCE CORPORATION  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)

| (In thousands)   | For the Three Months<br>Ended March 31, |           |
|--|---|-----------|
|  | 2011                                    | 2010      |
| Cash Flows From Operating Activities:                                  |   |           |
| Net income   | \$ 43,191                               | \$ 32,010 |
| Adjustments to reconcile cash provided by operating activities:        |   |           |
| Provision for credit losses  | 8,916                                   | 6,426     |
| Depreciation and amortization  | 2,488                                   | 3,248     |
| Loss on retirement of property and equipment                           | 4                                       | -         |
| Provision for deferred income taxes                                    | (5,377)                                 | (5,679)   |
| Stock-based compensation   | 591                                     | 1,183     |
| Change in operating assets and liabilities:                            |   |           |
| Increase in accounts payable and accrued liabilities                   | 21,959                                  | 25,776    |
| Decrease in income taxes receivable / increase in income taxes payable | 21,836                                  | 11,021    |
| Increase in other assets   | (7,537)                                 | (6,223)   |
| Net cash provided by operating activities                              | 86,071                                  | 67,762    |
| Cash Flows From Investing Activities:                                  |   |           |
| Increase in restricted cash and cash equivalents                       | (14,834)                                | (4,692)   |
| Purchases of restricted securities available for sale                  | (303)                                   | (407)     |
| Maturities of restricted securities available for sale                 | 305                                     | 449       |
| Principal collected on Loans receivable                                | 253,592                                 | 206,137   |
| Advances to Dealer-Partners  | (336,408)                               | (205,118) |
| Purchases of Consumer Loans  | (32,726)                                | (26,443)  |
| Accelerated payments of Dealer Holdback                                | (12,045)                                | (7,199)   |
| Payments of Dealer Holdback  | (15,574)                                | (12,170)  |
| Net (increase) decrease in other loans                                 | (230)                                   | 38        |
| Purchases of property and equipment                                    | (1,582)                                 | (781)     |
| Net cash used in investing activities                                  | (159,805)                               | (50,186)  |
| Cash Flows From Financing Activities:                                  |   |           |
| Borrowings under revolving secured line of credit                      | 489,000                                 | 99,900    |
| Repayments under revolving secured line of credit                      | (492,900)                               | (168,800) |
| Proceeds from secured financing  | 150,000                                 | -         |
| Repayments of secured financing  | (51,500)                                | (183,430) |
| Principal payments under mortgage note and capital lease obligations   | (58)                                    | (207)     |
| Proceeds from sale of senior notes                                     | 106,000                                 | 243,738   |
| Payments of debt issuance costs  | (3,028)                                 | (8,422)   |
| Repurchase of common stock   | (126,675)                               | (1,896)   |
| Proceeds from stock options exercised                                  | 1,915                                   | 19        |
| Tax benefits from stock-based compensation plans                       | 1,773                                   | 954       |
| Net cash provided by (used in) financing activities                    | 74,527                                  | (18,144)  |
| Net increase (decrease) in cash and cash equivalents                   | 793                                     | (568)     |
| Cash and cash equivalents, beginning of period                         | 3,792                                   | 2,170     |
| Cash and cash equivalents, end of period                               | \$ 4,585                                | \$ 1,602  |

Supplemental Disclosure of Cash Flow Information:



Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

|  |    |        |    |        |
|--|----|--------|----|--------|
| Cash paid during the period for interest     | \$ | 10,867 | \$ | 11,494 |
| Cash paid during the period for income taxes | \$ | 6,306  | \$ | 5,126  |

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“generally accepted accounting principles” or “GAAP”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The results of operations for interim periods are not necessarily indicative of actual results achieved for full fiscal years. The consolidated balance sheet as of December 31, 2010 has been derived from the audited financial statements at that date but does not include all the information and footnotes required by GAAP for complete financial statements. For further information, refer to the consolidated financial statements and footnotes thereto included in the Annual Report on Form 10-K for the year ended December 31, 2010 for Credit Acceptance Corporation (the “Company”, “Credit Acceptance”, “we”, “our” or “us”).

Certain amounts for prior periods have been reclassified to conform to the current presentation. We have changed the presentation of our consolidated statement of cash flows to reflect the increased significance of debt issuance costs. Under our current presentation, payments of debt issuance costs are presented as a separate financing activity and the related amortization is presented within operating activities as depreciation and amortization. Under our previous presentation, payments of debt issuance costs and the related amortization were presented as a net change in other assets within operating activities. We have also changed the presentation of our consolidated statement of cash flows to present advances to Dealer-Partners (as defined in Note 2) and accelerated payments of Dealer Holdback (as defined in Note 2) as separate investing activities. Under our previous presentation, advances to Dealer-Partners and accelerated payments of Dealer Holdback were presented as a combined investing activity.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

We have evaluated events and transactions occurring subsequent to the consolidated balance sheet date of March 31, 2011 for items that could potentially be recognized or disclosed in these financial statements. We did not identify any items which would require disclosure in or adjustment to the financial statements.

2. DESCRIPTION OF BUSINESS

Since 1972, Credit Acceptance has provided auto loans to consumers, regardless of their credit history. Our product is offered through a nationwide network of automobile dealers who benefit from sales of vehicles to consumers who otherwise could not obtain financing; from repeat and referral sales generated by these same customers; and from sales to customers responding to advertisements for our product, but who actually end up qualifying for traditional financing.

We refer to dealers who participate in our programs and who share our commitment to changing consumers’ lives as “Dealer-Partners”. Upon enrollment in our financing programs, the Dealer-Partner enters into a dealer servicing agreement with us that defines the legal relationship between Credit Acceptance and the Dealer-Partner. The dealer servicing agreement assigns the responsibilities for administering, servicing, and collecting the amounts due on retail installment contracts (referred to as “Consumer Loans”) from the Dealer-Partners to us. We are an indirect lender from a legal perspective, meaning the Consumer Loan is originated by the Dealer-Partner and assigned to us.

We have two programs: the Portfolio Program and the Purchase Program. Under the Portfolio Program, we advance money to Dealer-Partners (referred to as a “Dealer Loan”) in exchange for the right to service the underlying Consumer Loans. Under the Purchase Program, we buy the Consumer Loans from the Dealer-Partners (referred to as a “Purchased Loan”) and keep all amounts collected from the consumer. Dealer Loans and Purchased Loans are collectively referred to as “Loans”. The following table shows the percentage of Consumer Loans assigned to us based on unit volumes under each of the programs for each of the last five quarters:

| Quarter Ended      | Portfolio Program | Purchase Program |
|--------------------|-------------------|------------------|
| March 31, 2010     | 90.9%             | 9.1%             |
| June 30, 2010      | 90.5%             | 9.5%             |
| September 30, 2010 | 90.5%             | 9.5%             |
| December 31, 2010  | 91.8%             | 8.2%             |
| March 31, 2011     | 92.9%             | 7.1%             |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

2. DESCRIPTION OF BUSINESS – (Continued)

Portfolio Program

As payment for the vehicle, the Dealer-Partner generally receives the following:

- a down payment from the consumer;
- a non-recourse cash payment (“advance”) from us; and
- after the advance has been recovered by us, the cash from payments made on the Consumer Loan, net of certain collection costs and our servicing fee (“Dealer Holdback”).

We record the amount advanced to the Dealer-Partner as a Dealer Loan, which is classified within Loans receivable in our consolidated balance sheets. Cash advanced to Dealer-Partners is automatically assigned to the originating Dealer-Partner’s open pool of advances. We require Dealer-Partners to group advances into pools of at least 100 Consumer Loans. At the Dealer-Partner’s option, a pool containing at least 100 Consumer Loans can be closed and subsequent advances assigned to a new pool. All advances within a Dealer-Partner’s pool are secured by the future collections on the related Consumer Loans assigned to the pool. For Dealer-Partners with more than one pool, the pools are cross-collateralized so the performance of other pools is considered in determining eligibility for Dealer Holdback. We perfect our security interest in the Dealer Loans by taking possession of the Consumer Loans, which list us as lien holder on the vehicle title.

The dealer servicing agreement provides that collections received by us during a calendar month on Consumer Loans assigned by a Dealer-Partner are applied on a pool-by-pool basis as follows:

- First, to reimburse us for certain collection costs;
- Second, to pay us our servicing fee, which generally equals 20% of collections;
- Third, to reduce the aggregate advance balance and to pay any other amounts due from the Dealer-Partner to us; and
- Fourth, to the Dealer-Partner as payment of Dealer Holdback.

If the collections on Consumer Loans from a Dealer-Partner’s pool are not sufficient to repay the advance balance and any other amounts due to us, the Dealer-Partner will not receive Dealer Holdback.

Dealer-Partners have an opportunity to receive an accelerated Dealer Holdback payment at the time a pool of 100 or more Consumer Loans is closed. The amount paid to the Dealer-Partner is calculated using a formula that considers the forecasted collections and the advance balance on the closed pool.

Since typically the combination of the advance and the consumer’s down payment provides the Dealer-Partner with a cash profit at the time of sale, the Dealer-Partner’s risk in the Consumer Loan is limited. We cannot demand repayment of the advance from the Dealer-Partner except in the event the Dealer-Partner is in default of the dealer servicing agreement. Advances are made only after the consumer and Dealer-Partner have signed a Consumer Loan contract, we have received the original Consumer Loan contract and supporting documentation, and we have approved all of the related stipulations for funding. The Dealer-Partner can also opt to repurchase Consumer Loans that have been assigned to us under the Portfolio Program, at their discretion, for a fee.

For accounting purposes, the transactions described under the Portfolio Program are not considered to be loans to consumers. Instead, our accounting reflects that of a lender to the Dealer-Partner. The classification as a Dealer Loan

for accounting purposes is primarily a result of (1) the Dealer-Partner's financial interest in the Consumer Loan and (2) certain elements of our legal relationship with the Dealer-Partner.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

2. DESCRIPTION OF BUSINESS – (Concluded)

Purchase Program

The Purchase Program differs from our Portfolio Program in that the Dealer-Partner receives a one-time payment from us at the time of assignment to purchase the Consumer Loan instead of a cash advance at the time of assignment and future Dealer Holdback payments. For accounting purposes, the transactions described under the Purchase Program are considered to be originated by the Dealer-Partner and then purchased by us.

Program Enrollment

Dealer-Partners that enroll in our programs have two enrollment options available to them. The first enrollment option allows Dealer-Partners to assign Consumer Loans under the Portfolio Program and requires payment of an upfront, one-time fee of \$9,850. The second enrollment option allows Dealer-Partners to assign Consumer Loans under the Portfolio Program and requires payment of an upfront, one-time fee of \$1,950 and an agreement to allow us to keep 50% of their first accelerated Dealer Holdback payment. For all Dealer-Partners enrolling in our program after August 31, 2008, access to the Purchase Program is typically only granted after the first accelerated Dealer Holdback payment has been made under the Portfolio Program.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Business Segment Information

We currently operate in one reportable segment which represents our core business of offering auto loans, and related products and services to consumers through our network of Dealer-Partners. The consolidated financial statements reflect the financial results of our one reportable operating segment.

Loans Receivable and Allowance for Credit Losses

Consumer Loan Assignment. For accounting purposes, a Consumer Loan is considered to have been assigned to us after all of the following has occurred:

- the consumer and Dealer-Partner have signed a Consumer Loan contract;
- we have received the original Consumer Loan contract and supporting documentation;
- we have approved all of the related stipulations for funding; and
- we have provided funding to the Dealer-Partner in the form of either an advance under the Portfolio Program or one-time purchase payment under the Purchase Program.

Portfolio Segments and Classes. We are considered to be a lender to our Dealer-Partners for Consumer Loans assigned under our Portfolio Program and a purchaser of Consumer Loans assigned under our Purchase Program. As a result, our Loan portfolio consists of two portfolio segments: Dealer Loans and Purchased Loans. We have only one class of Consumer Loans assigned under our programs, which are retail installment contracts with deteriorated credit quality that were originated by Dealer-Partners to finance consumer purchases of vehicles and related ancillary products.

Dealer Loans. Amounts advanced to Dealer-Partners for Consumer Loans assigned under the Portfolio Program are recorded as Dealer Loans and are aggregated by Dealer-Partner for purposes of recognizing revenue and evaluating impairment. We account for Dealer Loans in a manner consistent with loans acquired with deteriorated credit quality. The outstanding balance of each Dealer Loan included in Loans receivable is comprised of the following:

- the aggregate amount of all cash advances paid;
- finance charges;
- Dealer Holdback payments;
- accelerated Dealer Holdback payments; and
- recoveries.

Less:

- collections (net of certain collection costs); and
- write-offs.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

An allowance for credit losses is maintained at an amount that reduces the net asset value (Dealer Loan balance less the allowance) to the value of forecasted future cash flows discounted at the yield established at the time of assignment. This allowance calculation is completed for each individual Dealer-Partner. The discounted value of future cash flows is comprised of estimated future collections on the Consumer Loans, less any estimated Dealer Holdback payments. We write off Dealer Loans once there are no forecasted future collections on any of the associated Consumer Loans, which generally occurs 120 months after the last Consumer Loan assignment.

Future collections on Dealer Loans are forecasted based on the historical performance of Consumer Loans with similar characteristics, adjusted for recent trends in payment patterns. Dealer Holdback is forecasted based on the expected future collections and current advance balance of each Dealer Loan. Cash flows from any individual Dealer Loan are often different than estimated cash flows at the time of assignment. If such difference is favorable, the difference is recognized prospectively into income over the remaining life of the Dealer Loan through a yield adjustment. If such difference is unfavorable, a provision for credit losses is recorded immediately as a current period expense and a corresponding allowance for credit losses is established. Because differences between estimated cash flows at the time of assignment and actual cash flows occur often, an allowance is required for a significant portion of our Dealer Loan portfolio. An allowance for credit losses does not necessarily indicate that a Dealer Loan is unprofitable, and in recent years, very seldom are cash flows from a Dealer Loan insufficient to repay the initial amounts advanced to the Dealer-Partner.

Purchased Loans. Amounts paid to Dealer-Partners for Consumer Loans assigned under the Purchase Program are recorded as Purchased Loans and are aggregated into pools based on the month of purchase for purposes of recognizing revenue and evaluating impairment. We account for Purchased Loans as loans acquired with deteriorated credit quality. The outstanding balance of each Purchased Loan pool included in Loans receivable is comprised of the following:

- the aggregate amount of all amounts paid during the month of purchase to purchase Consumer Loans from Dealer-Partners;

- finance charges; and
- recoveries.

Less:

- collections (net of certain collection costs); and
- write-offs.

An allowance for credit losses is maintained at an amount that reduces the net asset value (Purchased Loan pool balance less the allowance) to the value of forecasted future cash flows discounted at the yield established at the time of assignment. This allowance calculation is completed for each individual pool of Purchased Loans. The discounted value of future cash flows is comprised of estimated future collections on the pool of Purchased Loans. We write off pools of Purchased Loans once there are no forecasted future collections on any of the Purchased Loans included in the pool, which generally occurs 120 months after the month of purchase.

Future collections on Purchased Loans are forecasted based on the historical performance of Consumer Loans with similar characteristics, adjusted for recent trends in payment patterns. Cash flows from any individual pool of Purchased Loans are often different than estimated cash flows at the time of assignment. If such difference is



favorable, the difference is recognized prospectively into income over the remaining life of the pool of Purchased Loans through a yield adjustment. If such difference is unfavorable, a provision for credit losses is recorded immediately as a current period expense and a corresponding allowance for credit losses is established.

**Credit Risk.** Substantially all of the Consumer Loans assigned to us are made to individuals with impaired or limited credit histories or higher debt-to-income ratios than are permitted by traditional lenders. Consumer Loans made to these individuals generally entail a higher risk of delinquency, default and repossession and higher losses than loans made to consumers with better credit. Since most of our revenue and cash flows are generated from these Consumer Loans, our ability to accurately forecast Consumer Loan performance is critical to our business and financial results. At the time the Consumer Loan is submitted to us for assignment, we forecast future expected cash flows from the Consumer Loan. Based on these forecasts, an advance or one-time purchase payment is made to the related Dealer-Partner at a price designed to achieve an acceptable return on capital. We use a statistical model that considers a number of credit quality indicators to estimate the expected collection rate for each Consumer Loan at the time of assignment. Since all known, significant credit quality indicators have already been factored into our forecasts and pricing, we are not able to use any credit quality indicators to predict or explain variances in actual performance from our initial expectations. Any variances in performance from our initial expectations are the result of Consumer Loans performing differently than historical Consumer Loans with similar characteristics.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

When overall forecasted collection rates underperform our initial expectations for certain Consumer Loan assignment periods, the decline in forecasted collections has a more adverse impact on Purchased Loans than Dealer Loans. For Purchased Loans, the decline in forecasted collections is absorbed entirely by us. For Dealer Loans, the decline in the forecasted collections is substantially offset by a decline in forecasted payments of Dealer Holdback.

Forecast Methodology Changes and Modifications. For the three months ended March 31, 2011 and 2010, we did not make any methodology changes or significant modifications to our forecasts of future collections on Consumer Loans.

Reinsurance

VSC Re Company (“VSC Re”), our wholly-owned subsidiary, is engaged in the business of reinsuring coverage under vehicle service contracts sold to consumers by Dealer-Partners on vehicles financed by us. VSC Re currently reinsures vehicle service contracts that are underwritten by one of our two third party insurers. Vehicle service contract premiums, which represent the selling price of the vehicle service contract to the consumer, less commissions and certain administrative costs, are contributed to trust accounts controlled by VSC Re. These premiums are used to fund claims covered under the vehicle service contracts. VSC Re is a bankruptcy remote entity. As such, our exposure to fund claims is limited to the trust assets controlled by VSC Re and our net investment in VSC Re.

Premiums from the reinsurance of vehicle service contracts are recognized over the life of the policy in proportion to expected costs of servicing those contracts. Expected costs are determined based on our historical claims experience. Claims are expensed through a provision for claims in the period the claim was incurred. Capitalized acquisition costs are comprised of premium taxes and are amortized as general and administrative expense over the life of the contracts in proportion to premiums earned. A summary of reinsurance activity is as follows:

| (In thousands)                                | For the Three Months<br>Ended March 31, |           |
|---|---|-----------|
|   | 2011                                    | 2010      |
| Net assumed written premiums                  | \$ 14,386                               | \$ 10,270 |
| Net premiums earned                           | 8,543                                   | 7,705     |
| Provision for claims                          | 6,599                                   | 5,215     |
| Amortization of capitalized acquisition costs | 213                                     | 218       |

We are considered the primary beneficiary of the trusts and as a result, the trusts have been consolidated on our balance sheet. The trust assets and related reinsurance liabilities are as follows:

| (In thousands)     | Balance Sheet location                   | As of             |                      |
|--------------------|--|-------------------|----------------------|
|                    |  | March 31,<br>2011 | December<br>31, 2010 |
| Trust assets       | Restricted cash and cash equivalents     | \$ 35,228         | \$ 31,246            |
| Unearned premium   | Accounts payable and accrued liabilities | 30,600            | 24,757               |
| Claims reserve (1) | Accounts payable and accrued liabilities | 1,117             | 1,029                |

(1) The claims reserve is estimated based on historical claims experience.



NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

Our determination to consolidate the VSC Re trusts was based on the following:

- First, we determined that the trusts qualified as variable interest entities. The trusts have insufficient equity at risk as no parties to the trusts were required to contribute assets that provide them with any ownership interest.
- Next, we determined that we have variable interests in the trusts. We have a residual interest in the assets of the trusts, which is variable in nature, given that it increases or decreases based upon the actual loss experience of the related service contracts. In addition, VSC Re is required to absorb any losses in excess of the trusts' assets.
- Next, we evaluated the purpose and design of the trusts. The primary purpose of the trusts is to provide third party administrators ("TPAs") with funds to pay claims on vehicle service contracts and to accumulate and provide us with proceeds from investment income and residual funds.
- Finally, we determined that we are the primary beneficiary of the trusts. We control the amount of premium written and placed in the trusts through Consumer Loan assignments under our Programs, which is the activity that most significantly impacts the economic performance of the trusts. We have the right to receive benefits from the trusts that could potentially be significant. In addition, VSC Re has the obligation to absorb losses of the trusts that could potentially be significant.

Restricted Cash and Cash Equivalents

Restricted cash and cash equivalents increased to \$81.4 million as of March 31, 2011 from \$66.5 million as of December 31, 2010. The following table summarizes restricted cash and cash equivalents:

| (In thousands)   | As of             |                      |
|--|-------------------|----------------------|
|  | March 31,<br>2011 | December<br>31, 2010 |
| Cash collections related to secured financings                     | \$ 46,020         | \$ 35,160            |
| Cash held in trusts for future vehicle service contract claims (1) | 35,350            | 31,376               |
| <b>Total restricted cash and cash equivalents</b>                  | <b>\$ 81,370</b>  | <b>\$ 66,536</b>     |

- (1) The unearned premium and claims reserve associated with the trusts are included in accounts payable and accrued liabilities in the consolidated balance sheets. As of March 31, 2011, the outstanding balance includes \$35,228 related to VSC Re and \$122 related to a discontinued profit sharing arrangement. As of December 31, 2010, the outstanding balance includes \$31,246 related to VSC Re and \$130 related to a discontinued profit sharing arrangement.

Restricted Securities Available for Sale

Restricted securities available for sale consist of amounts held in a trust in accordance with a discontinued vehicle service contract profit sharing arrangement. We determine the appropriate classification of our investments in debt securities at the time of purchase and reevaluate such determinations at each balance sheet date. Debt securities for which we do not have the intent or ability to hold to maturity are classified as available for sale, and stated at fair value with unrealized gains and losses, net of income taxes included in the determination of comprehensive income and reported as a component of shareholders' equity.

Restricted securities available for sale consisted of the following:

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

(In thousands)

|  |        | As of March 31, 2011         |                               |                         |  |
|--|--------|------------------------------|-------------------------------|-------------------------|--|
|  | Cost   | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Estimated<br>Fair Value |  |
| US Government and agency securities            | \$ 149 | \$ 1                         | \$ -                          | \$ 150                  |  |
| Corporate bonds                                | 652    | 5                            | (1)                           | 656                     |  |
| Total restricted securities available for sale | \$ 801 | \$ 6                         | \$ (1)                        | \$ 806                  |  |

(In thousands)

|  |        | As of December 31, 2010      |                               |                         |  |
|--|--------|------------------------------|-------------------------------|-------------------------|--|
|  | Cost   | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Estimated<br>Fair Value |  |
| US Government and agency securities            | \$ 298 | \$ 3                         | \$ -                          | \$ 301                  |  |
| Corporate bonds                                | 504    | 5                            | (5)                           | 504                     |  |
| Total restricted securities available for sale | \$ 802 | \$ 8                         | \$ (5)                        | \$ 805                  |  |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Concluded)

The cost and estimated fair values of debt securities by contractual maturity were as follows (securities with multiple maturity dates are classified in the period of final maturity). Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

| (In thousands)  | March 31, 2011 |                         | As of<br>December 31, 2010 |                         |
|---|----------------|-------------------------|----------------------------|-------------------------|
|   | Cost           | Estimated<br>Fair Value | Cost                       | Estimated<br>Fair Value |
| <b>Contractual Maturity</b>                           |                |                         |                            |                         |
| Within one year                                       | \$ 245         | \$ 245                  | \$ 499                     | \$ 496                  |
| Over one year to five years                           | 556            | 561                     | 303                        | 309                     |
| <b>Total restricted securities available for sale</b> | <b>\$ 801</b>  | <b>\$ 806</b>           | <b>\$ 802</b>              | <b>\$ 805</b>           |

Deferred Debt Issuance Costs

As of March 31, 2011 and December 31, 2010, deferred debt issuance costs were \$17.2 million and \$15.6 million, respectively, and are included in other assets in the consolidated balance sheets. Expenses associated with the issuance of debt instruments are capitalized and amortized as interest expense over the term of the debt instrument using the effective interest method for term secured financings and Senior Notes (as defined below in Note 5) and the straight-line method for lines of credit and revolving secured financings.

New Accounting Updates

**Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts.** In October 2010, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2010-26, which amends Topic 944 (Financial Services – Insurance). ASU No. 2010-26 is intended to address diversity in practice regarding the interpretation of which costs relating to the acquisition of new or renewal insurance contracts qualify for deferral. The amendments specify which costs incurred in the acquisition of new and renewal contracts should be capitalized. ASU No. 2010-26 is effective for fiscal years beginning after December 15, 2011. While the guidance in this ASU is required to be applied prospectively upon adoption, retrospective application is also permitted (to all prior periods presented). Early adoption is also permitted, but only at the beginning of an entity’s annual reporting period. The adoption of guidance within ASU No. 2010-26 beginning on January 1, 2012 is not expected to have a material impact on our consolidated financial statements.

4. LOANS RECEIVABLE

Loans receivable consists of the following:

| (In thousands)              | As of March 31, 2011 |                    |              |
|-----------------------------|----------------------|--------------------|--------------|
|                             | Dealer<br>Loans      | Purchased<br>Loans | Total        |
| Loans receivable            | \$ 1,233,387         | \$ 254,969         | \$ 1,488,356 |
| Allowance for credit losses | (122,801)            | (13,067)           | (135,868)    |

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

|                       |              |            |              |
|-----------------------|--------------|------------|--------------|
| Loans receivable, net | \$ 1,110,586 | \$ 241,902 | \$ 1,352,488 |
|-----------------------|--------------|------------|--------------|

(In thousands)

As of December 31, 2010

|                             | Dealer<br>Loans | Purchased<br>Loans | Total        |
|-----------------------------|-----------------|--------------------|--------------|
| Loans receivable            | \$ 1,082,039    | \$ 262,842         | \$ 1,344,881 |
| Allowance for credit losses | (113,227)       | (13,641)           | (126,868)    |
| Loans receivable, net       | \$ 968,812      | \$ 249,201         | \$ 1,218,013 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

## 4. LOANS RECEIVABLE – (Concluded)

A summary of changes in Loans receivable is as follows:

| (In thousands)                          | For the Three Months Ended March 31,<br>2011 |                    |              |
|---|--|--------------------|--------------|
|   | Dealer<br>Loans                              | Purchased<br>Loans | Total        |
| Balance, beginning of period            | \$ 1,082,039                                 | \$ 262,842         | \$ 1,344,881 |
| New Consumer Loan assignments (1)       | 336,408                                      | 32,726             | 369,134      |
| Principal collected on Loans receivable | (208,459)                                    | (45,133)           | (253,592)    |
| Accelerated Dealer Holdback payments    | 12,045                                       | -                  | 12,045       |
| Dealer Holdback payments                | 15,574                                       | -                  | 15,574       |
| Transfers (2)                           | (4,596)                                      | 4,596              | -            |
| Write-offs                              | (351)  | (78)               | (429)        |
| Recoveries                              | 497  | 16                 | 513          |
| Net change in other loans               | 230  | -                  | 230          |
| Balance, end of period                  | \$ 1,233,387                                 | \$ 254,969         | \$ 1,488,356 |

| (In thousands)                          | For the Three Months Ended March 31,<br>2010 |                    |              |
|---|--|--------------------|--------------|
|   | Dealer<br>Loans                              | Purchased<br>Loans | Total        |
| Balance, beginning of period            | \$ 869,603                                   | \$ 297,955         | \$ 1,167,558 |
| New Consumer Loan assignments (1)       | 205,118                                      | 26,443             | 231,561      |
| Principal collected on Loans receivable | (161,991)                                    | (44,146)           | (206,137)    |
| Accelerated Dealer Holdback payments    | 7,199  | -                  | 7,199        |
| Dealer Holdback payments                | 12,170                                       | -                  | 12,170       |
| Transfers (2)                           | (6,143)                                      | 6,143              | -            |
| Write-offs                              | (1,388)                                      | (25)               | (1,413)      |
| Recoveries                              | 564  | 22                 | 586          |
| Net change in other loans               | (38)   | -                  | (38)         |
| Balance, end of period                  | \$ 925,094                                   | \$ 286,392         | \$ 1,211,486 |

(1) The Dealer Loans amount represents advances paid to Dealer-Partners on Consumer Loans assigned under our Portfolio Program. The Purchased Loans amount represents one-time payments made to Dealer-Partners to purchase Consumer Loans assigned under our Purchase Program.

(2) Under our Portfolio Program, certain events may result in Dealer-Partners forfeiting their rights to Dealer Holdback. We transfer the Dealer-Partner's outstanding Dealer Loan balance to Purchased Loans in the period this forfeiture occurs.

A summary of changes in the allowance for credit losses is as follows:

| (In thousands) | For the Three Months Ended March 31,<br>2011 |  |
|----------------|--|--|
|                | Total  |  |



Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

|                              | Dealer<br>Loans | Purchased<br>Loans |            |
|------------------------------|-----------------|--------------------|------------|
| Balance, beginning of period | \$ 113,227      | \$ 13,641          | \$ 126,868 |
| Provision for credit losses  | 9,428           | (512)              | 8,916      |
| Write-offs                   | (351)           | (78)               | (429)      |
| Recoveries                   | 497             | 16                 | 513        |
| Balance, end of period       | \$ 122,801      | \$ 13,067          | \$ 135,868 |

For the Three Months Ended March 31,  
2010

(In thousands)

|                              | Dealer<br>Loans | Purchased<br>Loans | Total      |
|------------------------------|-----------------|--------------------|------------|
| Balance, beginning of period | \$ 108,792      | \$ 8,753           | \$ 117,545 |
| Provision for credit losses  | 3,404           | 3,022              | 6,426      |
| Write-offs                   | (1,388)         | (25)               | (1,413)    |
| Recoveries                   | 564             | 22                 | 586        |
| Balance, end of period       | \$ 111,372      | \$ 11,772          | \$ 123,144 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

## 5. DEBT

We currently utilize the following primary forms of debt financing: (1) a revolving secured line of credit with a commercial bank syndicate; (2) revolving secured warehouse facilities with institutional investors; (3) asset-backed secured financings (“Term ABS”) with qualified institutional investors; and (4) 9.125% First Priority Senior Secured Notes due 2017 (“Senior Notes”). General information for each of our financing transactions in place as of March 31, 2011 is as follows:

(Dollars in thousands)

| Financings                               | Wholly-owned Subsidiary              | Issue Number | Close Date         | Maturity Date          | Financing Amount | Interest Rate as of March 31, 2011  |
|--|--------------------------------------|--------------|--------------------|------------------------|------------------|---|
| Revolving Secured Line of Credit         | n/a                                  | n/a          | June 9, 2010       | June 22, 2012          | \$ 170,000       | At our option, either the Eurodollar rate plus 225 basis points or the prime rate plus 125 basis points |
| Revolving Secured Warehouse Facility (1) | CAC Warehouse Funding Corp. II       | 2003-2       | June 16, 2010      | June 15, 2013 (2)      | \$ 325,000       | Commercial paper rate plus 350 basis points or LIBOR plus 450 basis points (4) (5)                      |
| Revolving Secured Warehouse Facility (1) | CAC Warehouse Funding III, LLC       | 2008-2       | September 10, 2010 | September 10, 2013 (6) | \$ 75,000        | Commercial paper rate plus 300 basis points or LIBOR plus 300 basis points (3) (4) (5)                  |
| Term ABS 2009-1 (1)                      | Credit Acceptance Funding LLC 2009-1 | 2009-1       | December 3, 2009   | May 15, 2011 (2)       | \$ 110,500       | Fixed rate  |
| Term ABS 2010-1 (1)                      | Credit Acceptance Funding LLC 2010-1 | 2010-1       | November 4, 2010   | October 15, 2012 (2)   | \$ 100,500       | Fixed rate  |
| Senior Notes                             | n/a                                  | n/a          | (7)                | February 1, 2017       | \$ 350,000       | Fixed rate  |

(1) Financing made available only to a specified subsidiary of the Company.

(2) Represents the revolving maturity date. The outstanding balance will amortize after the maturity date based on the cash flows of the contributed assets.

(3) A portion of the outstanding balance is a floating rate obligation that has been converted to a fixed rate obligation via an interest rate swap.

(4) The LIBOR rate is used if funding is not available from the commercial paper market.

(5) Interest rate cap agreements are in place to limit the exposure to increasing interest rates.

- (6) Represents the revolving maturity date. The outstanding balance will amortize after the revolving maturity date and any amounts remaining on September 10, 2014 will be due.
- (7) The close dates associated with the issuance of \$250.0 million and \$100.0 million of the Senior Notes occurred on February 1, 2010 and March 3, 2011, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

## 5. DEBT – (Continued)

Additional information related to the amounts outstanding on each facility is as follows:

| (In thousands)                                       | For the Three Months<br>Ended March 31, |            |
|--|---|------------|
|  | 2011                                    | 2010       |
| <b>Revolving Secured Line of Credit</b>              |   |            |
| Maximum outstanding balance                          | \$ 149,700                              | \$ 107,900 |
| Average outstanding balance                          | 86,538                                  | 44,533     |
| <b>Revolving Secured Warehouse Facility (2003-2)</b> |   |            |
| Maximum outstanding balance                          | \$ 180,600                              | \$ 152,600 |
| Average outstanding balance                          | 124,633                                 | 53,591     |
| <b>Revolving Secured Warehouse Facility (2008-2)</b> |   |            |
| Maximum outstanding balance                          | \$ 40,000                               | \$ 75,000  |
| Average outstanding balance                          | 35,489                                  | 75,000     |

| (Dollars in thousands)                               | As of             |                      |
|--|-------------------|----------------------|
|  | March 31,<br>2011 | December<br>31, 2010 |
| <b>Revolving Secured Line of Credit</b>              |                   |                      |
| Balance outstanding                                  | \$ 132,800        | \$ 136,700           |
| Letter of credit                                     | 500               | 500                  |
| Amount available for borrowing (1)                   | 36,700            | 32,800               |
| Interest rate  | 3.00%             | 3.03%                |
| <b>Revolving Secured Warehouse Facility (2003-2)</b> |                   |                      |
| Balance outstanding                                  | \$ 162,600        | \$ 49,100            |
| Amount available for borrowing (1)                   | 162,400           | 275,900              |
| Contributed eligible Loans                           | 229,678           | 83,652               |
| Interest rate  | 3.79%             | 3.82%                |
| <b>Revolving Secured Warehouse Facility (2008-2)</b> |                   |                      |
| Balance outstanding                                  | \$ 25,000         | \$ 40,000            |
| Amount available for borrowing (1)                   | 50,000            | 35,000               |
| Contributed eligible Loans                           | 57,646            | 70,950               |
| Interest rate  | 4.36%             | 3.94%                |
| <b>Term ABS 2009-1</b>                               |                   |                      |
| Balance outstanding                                  | \$ 110,500        | \$ 110,500           |
| Contributed eligible Loans                           | 142,507           | 142,490              |
| Interest rate  | 4.40%             | 4.40%                |

|                            |            |            |
|----------------------------|------------|------------|
| Term ABS 2010-1            |            |            |
| Balance outstanding        | \$ 100,500 | \$ 100,500 |
| Contributed eligible Loans | 127,112    | 127,054    |
| Interest rate              | 2.36%      | 2.36%      |
| Senior Notes               |            |            |
| Balance outstanding (2)    | \$ 350,455 | \$ 244,344 |
| Interest rate              | 9.13%      | 9.13%      |

(1) Availability may be limited by the amount of eligible Loans.

(2) The outstanding balance presented for the Senior Notes includes a net unamortized debt premium of \$0.5 million as of March 31, 2011 and unamortized debt discount of \$5.7 million as of December 31, 2010.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

5. DEBT – (Continued)

Senior Notes

We have outstanding \$350.0 million aggregate principal amount of our 9.125% First Priority Senior Secured Notes due 2017, \$100.0 million of which we issued on March 3, 2011 and \$250.0 million of which we issued on February 1, 2010. The Senior Notes are governed by an indenture, dated as of February 1, 2010, as amended and supplemented (the “Indenture”), among us, as the issuer; our subsidiaries Buyers Vehicle Protection Plan, Inc. and Vehicle Remarketing Services, Inc., as guarantors (the “Guarantors”); and U.S. Bank National Association, as trustee. The Senior Notes issued on March 3, 2011 have the same terms as the previously issued Senior Notes, other than issue price and issue date, and all of the Senior Notes are treated as a single class under the Indenture.

The Senior Notes mature on February 1, 2017 and bear interest at a rate of 9.125% per annum, computed on the basis of a 360-day year comprised of twelve 30-day months and payable semi-annually on February 1 and August 1 of each year, beginning on August 1, 2010. The Senior Notes issued on March 3, 2011 were issued at a price of 106.0% of their aggregate principal amount, resulting in gross proceeds of \$106.0 million, and a yield to maturity of 7.83% per annum. The Senior Notes issued on February 1, 2010 were issued at a price of 97.495% of their aggregate principal amount, resulting in gross proceeds of \$243.7 million, and a yield to maturity of 9.625% per annum. The premium with respect to the Senior Notes issued on March 3, 2011 and the discount with respect to the Senior Notes issued on February 1, 2010 are being amortized over the life of the Senior Notes using the effective interest method.

The Senior Notes are guaranteed on a senior secured basis by the Guarantors, which are also guarantors of obligations under our revolving secured line of credit facility. Other existing and future subsidiaries of ours may become guarantors of the Senior Notes. The Senior Notes and the Guarantors’ Senior Note guarantees are secured on a first-priority basis (subject to specified exceptions and permitted liens), together with all indebtedness outstanding from time to time under the revolving secured line of credit facility and, under certain circumstances, certain future indebtedness, by a security interest in substantially all of our assets and those of the Guarantors, subject to certain exceptions such as real property, cash (except to the extent it is deposited with the collateral agent), certain leases, and equity interests of our subsidiaries (other than those of specified subsidiaries including the Guarantors). Our assets and those of the Guarantors securing the Senior Notes and the Senior Note guarantees will not include our assets transferred to special purpose subsidiaries in connection with securitization transactions and will generally be the same as the collateral securing indebtedness under the revolving secured line of credit facility and, under certain circumstances, certain future indebtedness, subject to certain limited exceptions as provided in the security and intercreditor agreements related to the revolving secured line of credit facility.

Revolving Secured Line of Credit Facility

Borrowings under the revolving secured line of credit facility, including any letters of credit issued under the facility, are subject to a borrowing-base limitation. This limitation equals 80% of the net book value of Loans, less a hedging reserve (not exceeding \$1.0 million), and the amount of other debt secured by the collateral which secures the revolving secured line of credit facility. Borrowings under the revolving secured line of credit facility agreement are secured by a lien on most of our assets. We must pay quarterly fees on the amount of the facility.

Revolving Secured Warehouse Facilities

We have two revolving secured warehouse facilities that are provided to our wholly-owned subsidiaries. One is a \$325.0 million facility with an institutional investor and the other is a \$75.0 million facility with another institutional investor.

Under both revolving secured warehouse facilities we can contribute Loans to our wholly-owned subsidiaries in return for cash and equity in each subsidiary. In turn, each subsidiary pledges the Loans as collateral to institutional investors to secure financing that will fund the cash portion of the purchase price of the Loans. The financing provided to each subsidiary under the applicable facility is limited to the lesser of 80% of the net book value of the contributed Loans or the facility limit.

The financings create indebtedness for which the subsidiaries are liable and which is secured by all the assets of each subsidiary. Such indebtedness is non-recourse to us, even though we are consolidated for financial reporting purposes with the subsidiaries. Because the subsidiaries are organized as legal entities separate from us, their assets (including the conveyed Loans) are not available to our creditors.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

5. DEBT – (Continued)

Interest on borrowings under the \$325.0 million revolving secured warehouse facility has been limited through interest rate cap agreements to a maximum rate of 6.75% plus the spread over the LIBOR rate or the commercial paper rate, as applicable. Interest on borrowings for a portion of the \$75.0 million revolving secured warehouse facility has also been limited through interest rate cap agreements to a maximum rate of 6.75% plus the spread over the LIBOR rate or the commercial paper rate, as applicable. We have also entered into an interest rate swap to convert \$25.0 million of the \$75.0 million revolving secured warehouse facility into fixed rate debt bearing an interest rate of 4.36%. For additional information, see Note 6 of these consolidated financial statements.

The subsidiaries pay us a monthly servicing fee equal to 6% of the collections received with respect to the conveyed Loans. The fee is paid out of the collections. Except for the servicing fee and holdback payments due to Dealer-Partners, if a facility is amortizing, we do not have any rights in any portion of such collections until all outstanding principal, accrued and unpaid interest, fees and other related costs have been paid in full. If a facility is not amortizing, the applicable subsidiary may be entitled to retain a portion of such collections provided that the borrowing base requirements of the facility are satisfied.

Term ABS Financings

In 2009 and 2010, two of our wholly-owned subsidiaries (the “Funding LLCs”), each completed a secured financing transaction. In connection with these transactions, we contributed Loans on an arms-length basis to each Funding LLC for cash and the sole membership interest in that Funding LLC. In turn, each Funding LLC contributed the Loans to a respective trust that issued notes to qualified institutional investors. The Term ABS 2010-1 and 2009-1 transactions consist of three classes of notes. The Class A Notes for each Term ABS financing were rated by S&P and DBRS, Inc. and the Class B Notes for each Term ABS financing were rated by S&P. The Class C Notes for each Term ABS financing do not bear interest, were not rated and have been retained by us.

Each financing at the time of issuance has a specified revolving period during which we may be required, and are likely, to convey additional Loans to each Funding LLC. Each Funding LLC will then convey the Loans to their respective trust. At the end of the revolving period, the debt outstanding under each financing will begin to amortize.

The financings create indebtedness for which the trusts are liable and which is secured by all the assets of each trust. Such indebtedness is non-recourse to us, even though we are consolidated for financial reporting purposes with the trusts and the Funding LLCs. Because the Funding LLCs are organized as legal entities separate from us, their assets (including the conveyed Loans) are not available to our creditors. We receive a monthly servicing fee on each financing equal to 6% of the collections received with respect to the conveyed Loans. The fee is paid out of the collections. Except for the servicing fee and Dealer Holdback payments due to Dealer-Partners, if a facility is amortizing, we do not have any rights in any portion of such collections until all outstanding principal, accrued and unpaid interest, fees and other related costs have been paid in full. If a facility is not amortizing, the applicable subsidiary may be entitled to retain a portion of such collections provided that the borrowing base requirements of the facility are satisfied. However, in our capacity as servicer of the Loans, we do have a limited right to exercise a “clean-up call” option to purchase Loans from the Funding LLCs and/or the trusts under certain specified circumstances. Alternatively, when a trust’s underlying indebtedness is paid in full, either through collections or through a prepayment of the indebtedness, the trust is to pay any remaining collections over to its Funding LLC as the sole beneficiary of the trust. The collections will then be available to be distributed to us as the sole member of the respective Funding LLC.



The table below sets forth certain additional details regarding the outstanding Term ABS Financings:

(Dollars in thousands)

| Term ABS Financings | Issue Number | Close Date       | Net Book Value of Dealer Loans Conveyed at Closing | Revolving Period                        | Expected Annualized Rates (1) |
|---------------------|--------------|------------------|--|---|-------------------------------|
| Term ABS 2009-1     | 2009-1       | December 3, 2009 | \$ 142,301   | 18 months<br>(Through May 15, 2011)     | 5.2%                          |
| Term ABS 2010-1     | 2010-1       | November 4, 2010 | \$ 126,751   | 24 months<br>(Through October 15, 2012) | 3.1%                          |

(1) Includes underwriter's fees and other costs.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

5. DEBT – (Concluded)

Debt Covenants

As of March 31, 2011, we were in compliance with all our debt covenants relating to the revolving secured line of credit facility, including those that require the maintenance of certain financial ratios and other financial conditions. These covenants require a minimum ratio of our assets to debt and a minimum ratio of our earnings before interest, taxes and non-cash expenses to fixed charges. These covenants also limit the maximum ratio of our funded debt to tangible net worth. Additionally, we must maintain consolidated net income of not less than \$1 for the two most recently ended fiscal quarters. Some of these debt covenants may indirectly limit the repurchase of common stock or payment of dividends on common stock.

Our revolving secured warehouse facilities and Term ABS financings also contain covenants that measure the performance of the contributed assets. As of March 31, 2011, we were in compliance with all such covenants. As of the end of the quarter, we were also in compliance with our covenants under the Indenture. The Indenture includes covenants that limit the maximum ratio of our funded debt to tangible net worth and also require a minimum collateral coverage ratio.

6. DERIVATIVE AND HEDGING INSTRUMENTS

Interest Rate Caps. We purchase interest rate cap agreements to manage the interest rate risk on certain borrowings.

As of March 31, 2011, we had interest rate cap agreements to manage the interest rate risk on our \$325.0 million revolving secured warehouse facility with various maturities between August 2011 and May 2012. As of December 31, 2010, we had interest rate cap agreements to manage the interest rate risk on our \$325.0 million revolving secured warehouse facility with various maturities between February 2011 and May 2012. As of March 31, 2011 and December 31, 2010, we also had an interest rate cap agreement that matures on September 19, 2013 to manage the interest rate risk on a portion of our \$75.0 million revolving secured warehouse facility. These instruments limit the interest rate on both revolving secured warehouse facilities to 6.75% plus the spread over the LIBOR rate or the commercial paper rate, as applicable.

The interest rate caps have not been designated as hedging instruments.

Interest Rate Swaps. As of March 31, 2011 and December 31, 2010, we had an interest rate swap outstanding which matures in August 2011 to convert \$25.0 million of the \$75.0 million revolving secured warehouse facility into fixed rate debt, bearing an interest rate of 4.36%. This interest rate swap has been designated as a cash flow hedging instrument.

As of March 31, 2011, we had minimal exposure to credit loss on the outstanding interest rate swap. We do not believe that any reasonably likely change in interest rates would have a materially adverse effect on our financial position, our results of operations or our cash flows.

Information related to the fair values of derivative instruments in our consolidated balance sheets as of March 31, 2011 and December 31, 2010 is as follows:

(In thousands)

Fair Value as of

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

|   | Balance Sheet location                   | March 31,<br>2011 | December<br>31, 2010 |
|---|--|-------------------|----------------------|
| Derivatives designated as hedging instruments     |  |                   |                      |
| Liability Derivatives                             |  |                   |                      |
| Interest rate swap                                | Accounts payable and accrued liabilities | \$ 115            | \$ 176               |
| Derivatives not designated as hedging instruments |  |                   |                      |
| Asset Derivatives                                 |  |                   |                      |
| Interest rate caps                                | Other assets                             | \$ 35             | \$ 56                |
| Total Derivatives                                 |  |                   |                      |
| Total Asset Derivatives                           |  | \$ 35             | \$ 56                |
| Total Liability Derivatives                       |  | \$ 115            | \$ 176               |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

6. DERIVATIVE AND HEDGING INSTRUMENTS – (Concluded)

Information related to the effect of derivative instruments designated as hedging instruments in our consolidated financial statements is as follows:

(In thousands)

| Derivatives in Cash Flow Hedging Relationships | (Loss) / Gain Recognized in OCI on Derivative (Effective Portion) For the Three Months Ended March 31, |       | Location         | (Loss) / Gain Reclassified from Accumulated OCI into Income (Effective Portion) For the Three Months Ended March 31, |          |
|--|--|-------|------------------|--|----------|
|  | 2011   | 2010  |                  | 2011   | 2010     |
| Interest rate swap                             | \$ (8)   | \$ 49 | Interest expense | \$ (69)  | \$ (440) |

As of March 31, 2011, we expect to reclassify losses of \$0.1 million from accumulated other comprehensive income into income during the next twelve months.

Information related to the effect of derivative instruments not designated as hedging instruments on our consolidated statements of income for the three months ended March 31, 2011 and 2010 is as follows:

(In thousands)

| Derivatives Not Designated as Hedging Instruments | Location         | Amount of (Loss) / Gain Recognized in Income on Derivatives For the Three Months Ended March 31, |          |
|---|------------------|--|----------|
|   |                  | 2011   | 2010     |
| Interest rate caps                                | Interest expense | \$ (20)  | \$ (76)  |
| Interest rate swap                                | Interest expense | -  | (590)    |
| Total   |                  | \$ (20)  | \$ (666) |

7. FAIR VALUE OF FINANCIAL INSTRUMENTS

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate their value.

**Cash and Cash Equivalents and Restricted Cash and Cash Equivalents.** The carrying amount of cash and cash equivalents and restricted cash and cash equivalents approximate their fair value due to the short maturity of these instruments.

**Restricted Securities Available for Sale.** Restricted securities consist of amounts held in trusts by TPAs to pay claims on vehicle service contracts. Securities for which we do not have the intent or ability to hold to maturity are classified as available for sale and stated at fair value. The fair value of restricted securities are based on quoted market values.

Net Investment in Loans Receivable. Loans receivable, net represents our net investment in Consumer Loans. The fair value is determined by calculating the present value of future Loan payment inflows and Dealer Holdback outflows estimated by us utilizing a discount rate comparable with the rate used to calculate our allowance for credit losses.

Derivative Instruments. The fair value of interest rate caps and interest rate swaps are based on quoted prices for similar instruments in active markets, which are influenced by a number of factors, including interest rates, notional amount of the derivative, and number of months until maturity.

Liabilities. The fair value of debt is determined using quoted market prices, if available, or calculated using the estimated value of each debt instrument based on current rates offered to us for debt with similar maturities.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

## 7. FAIR VALUE OF FINANCIAL INSTRUMENTS – (Concluded)

A comparison of the carrying value and estimated fair value of these financial instruments is as follows:

| (In thousands)                           | March 31, 2011     |                         | As of<br>December 31, 2010 |                         |
|--|--------------------|-------------------------|----------------------------|-------------------------|
|  | Carrying<br>Amount | Estimated<br>Fair Value | Carrying<br>Amount         | Estimated<br>Fair Value |
| <b>Assets</b>                            |                    |                         |                            |                         |
| Cash and cash equivalents                | \$ 4,585           | \$ 4,585                | \$ 3,792                   | \$ 3,792                |
| Restricted cash and cash equivalents     | 81,370             | 81,370                  | 66,536                     | 66,536                  |
| Restricted securities available for sale | 806                | 806                     | 805                        | 805                     |
| Net investment in Loans receivable       | 1,352,488          | 1,365,369               | 1,218,013                  | 1,224,830               |
| Derivative instruments                   | 35                 | 35                      | 56                         | 56                      |
| <b>Liabilities</b>                       |                    |                         |                            |                         |
| Revolving secured line of credit         | \$ 132,800         | \$ 132,800              | \$ 136,700                 | \$ 136,700              |
| Secured financing                        | 398,600            | 400,088                 | 300,100                    | 302,377                 |
| Mortgage note                            | 4,465              | 4,465                   | 4,523                      | 4,523                   |
| Senior notes                             | 350,455            | 378,188                 | 244,344                    | 261,250                 |
| Derivative instruments                   | 115                | 115                     | 176                        | 176                     |

Fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. We group assets and liabilities at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1 Valuation is based upon quoted prices for identical instruments traded in active markets.

Level 2 Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3 Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates or assumptions that market participants would use in pricing the asset or liability.

The following table provides the fair value measurements of applicable assets and liabilities, measured at fair value on a recurring basis, as of March 31, 2011 and December 31, 2010:

| (In thousands)                              | As of March 31, 2011 |         |                     | As of December 31, 2010 |         |                     |
|---|----------------------|---------|---------------------|-------------------------|---------|---------------------|
|   | Level 1              | Level 2 | Total<br>Fair Value | Level 1                 | Level 2 | Total<br>Fair Value |
| <b>Assets</b>                               |                      |         |                     |                         |         |                     |
| Restricted securities available<br>for sale | \$ 806               | \$ -    | \$ 806              | \$ 805                  | \$ -    | \$ 805              |

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

|                        |      |        |        |      |        |        |
|------------------------|------|--------|--------|------|--------|--------|
| Derivative instruments | -    | 35     | 35     | -    | 56     | 56     |
| <b>Liabilities</b>     |      |        |        |      |        |        |
| Derivative instruments | \$ - | \$ 115 | \$ 115 | \$ - | \$ 176 | \$ 176 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

## 8. RELATED PARTY TRANSACTIONS

In the normal course of our business, affiliated Dealer-Partners assign Consumer Loans to us under the Portfolio and Purchase Programs. Dealer Loans and Purchased Loans with affiliated Dealer-Partners are on the same terms as those with non-affiliated Dealer-Partners. Affiliated Dealer-Partners are comprised of Dealer-Partners owned or controlled by: (1) our majority shareholder and Chairman; and (2) a member of the Chairman's immediate family.

Affiliated Dealer Loan balances were \$7.5 million and \$9.0 million as of March 31, 2011 and December 31, 2010, respectively. Affiliated Dealer Loan balances were 0.6% and 0.8% of total consolidated Dealer Loan balances as of March 31, 2011 and December 31, 2010, respectively. A summary of related party Loan activity is as follows:

| (In thousands)                       | For the Three Months Ended March 31,     |                      |  |                      |
|--------------------------------------|--|----------------------|--|----------------------|
|                                      | 2011                                     |                      | 2010                                     |                      |
|                                      | Affiliated<br>Dealer-Partner<br>activity | % of<br>consolidated | Affiliated<br>Dealer-Partner<br>activity | % of<br>consolidated |
| Dealer Loan revenue                  | \$ 545                                   | 0.6%                 | \$ 847                                   | 1.2%                 |
| New Consumer Loan assignments (1)    | 347                                      | 0.1%                 | 1,498                                    | 0.6%                 |
| Accelerated Dealer Holdback payments | 24                                       | 0.2%                 | 101                                      | 1.4%                 |
| Dealer Holdback payments             | 465                                      | 3.0%                 | 590                                      | 4.9%                 |

(1) Represents advances paid to Dealer-Partners on Consumer Loans assigned under our Portfolio Program and one-time payments made to Dealer-Partners to purchase Consumer Loans assigned under our Purchase Program.

Our majority shareholder and Chairman has indirect control over entities that, in the past, offered secured lines of credit to automobile dealers, and has the right or obligation to reacquire these entities under certain circumstances until December 31, 2014 or the repayment of the related purchase money note.

## 9. INCOME TAXES

A reconciliation of the U.S. federal statutory rate to our effective tax rate, excluding the results of the discontinued United Kingdom operations, is as follows:

|  | For the Three Months<br>Ended March 31, |       |
|--|---|-------|
|  | 2011                                    | 2010  |
| U.S. federal statutory rate  | 35.0%                                   | 35.0% |
| State income taxes   | 1.7%                                    | 2.1%  |
| Changes in reserve for uncertain tax positions as a result of settlements and lapsed statutes and related interest | -1.0%                                   | 1.6%  |
| Other  | 0.1%                                    | 0.3%  |
| Effective tax rate   | 35.8%                                   | 39.0% |

The differences between the U.S. federal statutory rate and our effective tax rate are primarily due to state income taxes and reserves for uncertain tax positions and related interest that are included in the provision for income taxes.



The decrease in the effective tax rate for the three months ended March 31, 2011, as compared to the same period in 2010, is primarily due to changes in the reserve for uncertain tax positions. During the first quarter of 2010, we increased our reserve for uncertain tax positions related to an ongoing dispute with the IRS. This additional reserve increased our effective tax rate for the period. During the first quarter of 2011, we resolved a portion of this dispute, which allowed us to reverse a portion of the amount previously provided.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

10. CAPITAL TRANSACTIONS

Net Income Per Share

Basic net income per share has been computed by dividing net income by the basic number of weighted average shares outstanding. Diluted net income per share has been computed by dividing net income by the diluted number of weighted average shares outstanding using the treasury stock method. The share effect is as follows:

| (In thousands)   | For the Three Months<br>Ended March 31, |        |
|--|---|--------|
|  | 2011                                    | 2010   |
| Weighted average shares outstanding:                           |   |        |
| Common shares  | 26,833                                  | 30,842 |
| Vested restricted stock units                                  | 363                                     | 200    |
| Basic number of weighted average shares outstanding            | 27,196                                  | 31,042 |
| Dilutive effect of stock options                               | 174                                     | 368    |
| Dilutive effect of restricted stock and restricted stock units | 119                                     | 174    |
| Dilutive number of weighted average shares outstanding         | 27,489                                  | 31,584 |

For the three months ended March 31, 2011, there were 8,842 shares of restricted stock outstanding excluded from the calculation of diluted net income per share because the impact would have been anti-dilutive. For the three months ended March 31, 2010, there were no stock options, restricted stock or restricted stock units that would have been anti-dilutive.

Stock Repurchases

During the first quarter of 2011, we commenced a tender offer to repurchase 1.9 million shares of our common stock at a price of \$65.625 per share. Upon expiration of the tender offer during the first quarter of 2011, we repurchased 1.9 million common shares at a cost of \$125.0 million, which included 1.3 million shares beneficially owned by Donald A. Foss, our Chairman of the Board, and 0.5 million shares beneficially owned by the trustee of certain grantor retained annuity trusts created by Mr. Foss. We financed the repurchase of our common stock in the tender offer using the proceeds from the issuance of \$100.0 million of Senior Notes and by borrowing under our \$170.0 million revolving secured line of credit facility.

Stock Compensation Plans

Pursuant to our Amended and Restated Incentive Compensation Plan (the "Incentive Plan"), the number of shares reserved for granting of restricted stock, restricted stock units, stock options, and performance awards to team members, officers, directors, and contractors at any time prior to April 6, 2019 is 1.5 million shares. The shares available for future grants under the Incentive Plan totaled 316,560 as of March 31, 2011.

A summary of the restricted stock activity under the Incentive Plan for the three months ended March 31, 2011 and 2010 is presented below:

|                |                  |
|----------------|------------------|
| (In thousands) | Number of Shares |
|----------------|------------------|

| Restricted Stock              | For the Three Months<br>Ended March 31, |       |
|-------------------------------|---|-------|
|                               | 2011                                    | 2010  |
| Outstanding Beginning Balance | 112                                     | 242   |
| Granted                       | 9                                       | 19    |
| Vested                        | (63)                                    | (142) |
| Forfeited                     | (3)                                     | -     |
| Outstanding Ending Balance    | 55                                      | 119   |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)  
(UNAUDITED)

## 10. CAPITAL TRANSACTIONS – (Concluded)

A summary of the restricted stock unit activity under the Incentive Plan for the three months ended March 31, 2011 and 2010 is presented below:

(In thousands,  
except per share  
data)

| Restricted<br>Stock Units                 | Nonvested                              |   | Number of<br>Restricted<br>Stock Units | Vested  |       | Total<br>Number of<br>Restricted<br>Stock Units |
|---|--|---|--|---|-------|---|
|   | Number of<br>Restricted<br>Stock Units | Weighted<br>Average<br>Grant-Date Fair<br>Value Per Share |  | Weighted<br>Average<br>Grant-Date Fair<br>Value Per Share |       |   |
| Outstanding as<br>of December 31,<br>2010 | 521                                    | \$ 19.99  | 270                                    | \$ 22.94  | 791   |   |
| Granted                                   | 5                                      | 62.20   | -                                      | -   | 5 (1) |   |
| Vested                                    | (158)                                  | 20.99   | 158                                    | 20.99   | -(2)  |   |
| Outstanding as<br>of March 31,<br>2011    | 368                                    | \$ 20.13  | 428                                    | \$ 22.22  | 796   |   |

(In thousands,  
except per share  
data)

| Restricted<br>Stock Units                 | Nonvested                              |   | Number of<br>Restricted<br>Stock Units | Vested  |        | Total<br>Number of<br>Restricted<br>Stock Units |
|---|--|---|--|---|--------|---|
|   | Number of<br>Restricted<br>Stock Units | Weighted<br>Average<br>Grant-Date Fair<br>Value Per Share |  | Weighted<br>Average<br>Grant-Date Fair<br>Value Per Share |        |   |
| Outstanding as<br>of December 31,<br>2009 | 648                                    | \$ 19.35  | 120                                    | \$ 26.30  | 768    |   |
| Granted                                   | 33                                     | 39.89   | -                                      | -   | 33 (3) |   |
| Vested                                    | (150)                                  | 20.24   | 150                                    | 20.24   | -(4)   |   |
| Outstanding as<br>of March 31,<br>2010    | 531                                    | \$ 20.36  | 270                                    | \$ 22.94  | 801    |   |

(1) The distribution date of vested restricted stock units is February 22, 2018.

(2) The distribution date of vested restricted stock units is February 22, 2014 for 60 restricted stock units, February 22, 2016 for 90 restricted stock units and February 22, 2017 for 8 restricted stock units.

(3) The distribution date of vested restricted stock units is February 22, 2017.

(4) The distribution date of vested restricted stock units is February 22, 2014 for 60 restricted stock units and February 22, 2016 for 90 restricted stock units.

Stock compensation expense consists of the following:

| (In thousands)         | For the Three Months<br>Ended March 31, |          |
|------------------------|---|----------|
|                        | 2011                                    | 2010     |
| Restricted stock       | \$ 216                                  | \$ 334   |
| Restricted stock units | 375                                     | 849      |
| Total                  | \$ 591                                  | \$ 1,183 |

While the restricted stock units are expected to vest in equal, annual installments over a five-year period, the related stock compensation expense is not recognized on a straight-line basis over this period. Each installment is accounted for as a separate award and as a result, the fair value of each installment is recognized as stock compensation expense on a straight-line basis over the related vesting period.

#### 11. COMPREHENSIVE INCOME

Our comprehensive income information is set forth below:

| (In thousands)  | For the Three Months<br>Ended March 31, |           |
|---|---|-----------|
|   | 2011                                    | 2010      |
| Net income  | \$ 43,191                               | \$ 32,010 |
| Unrealized gain (loss) on securities available for sale, net of tax | 2                                       | (5)       |
| Unrealized gain on interest rate swap, net of tax                   | 39                                      | 309       |
| Comprehensive income  | \$ 43,232                               | \$ 32,314 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONCLUDED)  
(UNAUDITED)

12. LITIGATION AND CONTINGENT LIABILITIES

In the normal course of business and as a result of the customer-oriented nature of the industry in which we operate, industry participants are frequently subject to various customer claims and litigation seeking damages and statutory penalties. The claims allege, among other theories of liability, violations of state, federal and foreign truth-in-lending, credit availability, credit reporting, customer protection, warranty, debt collection, insurance and other customer-oriented laws and regulations, including claims seeking damages for physical and mental damages relating to our repossession and sale of the customer's vehicle and other debt collection activities. As the assignee of Consumer Loans originated by Dealer-Partners, we may also be named as a co-defendant in lawsuits filed by customers principally against Dealer-Partners. We may also have disputes and litigation with Dealer-Partners. The claims may allege, among other theories of liability, that we breached its dealer servicing agreement. Many of these cases are filed as purported class actions and seek damages in large dollar amounts. An adverse ultimate disposition in any such action could have a material adverse impact on our financial position, liquidity and results of operations.

On December 3, 2010, we received a civil investigative demand from the Missouri Attorney General Office relating to our practices regarding collections from Missouri consumers who claim to have not received title from the Dealer-Partner at the time of their purchase. On January 24, 2011, we provided our response and are in continued discussions with the Attorney General with respect to the demand for information. We are cooperating with the inquiry.

## 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 Item 8 - Financial Statements and Supplementary Data, of our 2010 Annual Report on Form 10-K, as well as Item 1- Consolidated Financial Statements, of this Form 10-Q, which is incorporated herein by reference.

### Overview

We provide auto loans to consumers regardless of their credit history. Our product is offered through a nationwide network of automobile dealers who benefit from sales of vehicles to consumers who otherwise could not obtain financing; from repeat and referral sales generated by these same customers; and from sales to customers responding to advertisements for our product, but who actually end up qualifying for traditional financing.

For the three months ended March 31, 2011, consolidated net income was \$43.2 million, or \$1.57 per diluted share, compared to \$32.0 million, or \$1.01 per diluted share, for the same period in 2010. The growth in 2011 consolidated net income was primarily due to an increase in the size of our Loan portfolio.

### Critical Success Factors

Critical success factors include our ability to access capital on acceptable terms, accurately forecast Consumer Loan performance, and maintain or grow Consumer Loan volume at the level and on the terms that we anticipate, with an objective to maximize economic profit. Economic profit is a financial metric we use to evaluate our financial results and determine incentive compensation. Economic profit measures how efficiently we utilize our total capital, both debt and equity, and is a function of the return on capital in excess of the cost of capital and the amount of capital invested in the business.

### Access to Capital

Our strategy for accessing capital on acceptable terms needed to maintain and grow the business is to: (1) maintain consistent financial performance; (2) maintain modest financial leverage; and (3) maintain multiple funding sources. Our funded debt to equity ratio is 2.2:1 as of March 31, 2011. We currently utilize the following primary forms of debt financing: (1) a revolving secured line of credit with a commercial bank syndicate; (2) revolving secured warehouse facilities with institutional investors; (3) Term ABS financings with qualified institutional investors; and (4) 9.125% First Priority Senior Secured Notes due 2017 (“Senior Notes”).

### Consumer Loan Performance

At the time a Consumer Loan is submitted to us for assignment, we forecast future expected cash flows from the Consumer Loan. Based on these forecasts, an advance or one-time purchase payment is made to the related Dealer-Partner at a price designed to achieve an acceptable return on capital. If Consumer Loan performance equals or exceeds our original expectation, it is likely our target return on capital will be achieved.

We use a statistical model to estimate the expected collection rate for each Consumer Loan at the time of assignment. We continue to evaluate the expected collection rate of each Consumer Loan subsequent to assignment. Our evaluation becomes more accurate as the Consumer Loans age, as we use actual performance data in our forecast. By comparing our current expected collection rate for each Consumer Loan with the rate we projected at

the time of assignment, we are able to assess the accuracy of our initial forecast. The following table compares our forecast of Consumer Loan collection rates as of March 31, 2011, with the forecasts as of December 31, 2010, and at the time of assignment, segmented by year of assignment:

| Consumer Loan Assignment Year | Forecasted Collection Percentage as of |                   |                  | Variance in Forecasted Collection Percentage from |                  |
|-------------------------------|--|-------------------|------------------|---|------------------|
|                               | March 31, 2011                         | December 31, 2010 | Initial Forecast | December 31, 2010                                 | Initial Forecast |
| 2002                          | 70.5%                                  | 70.5%             | 67.9%            | 0.0%  | 2.6%             |
| 2003                          | 73.7%                                  | 73.7%             | 72.0%            | 0.0%  | 1.7%             |
| 2004                          | 73.0%                                  | 73.0%             | 73.0%            | 0.0%  | 0.0%             |
| 2005                          | 73.7%                                  | 73.7%             | 74.0%            | 0.0%  | -0.3%            |
| 2006                          | 70.2%                                  | 70.2%             | 71.4%            | 0.0%  | -1.2%            |
| 2007                          | 68.0%                                  | 67.9%             | 70.7%            | 0.1%  | -2.7%            |
| 2008                          | 70.0%                                  | 69.9%             | 69.7%            | 0.1%  | 0.3%             |
| 2009                          | 78.6%                                  | 78.5%             | 71.9%            | 0.1%  | 6.7%             |
| 2010                          | 75.4%                                  | 75.8%             | 73.6%            | -0.4%   | 1.8%             |



Consumer Loans assigned in 2002, 2003, 2009 and 2010 have yielded forecasted collection results materially better than our initial estimates, while Consumer Loans assigned in 2006 and 2007 have yielded forecasted collection results materially worse than our initial estimates. For 2004, 2005 and 2008, actual results have been very close to our initial estimates. During the first quarter of 2011, forecasted collection rates decreased for Consumer Loans assigned in 2010, and were generally consistent with expectations at the start of the period for the other assignment years.

Forecasting collection rates precisely at Loan inception is difficult. With this in mind, we establish advance rates that are intended to allow us to achieve acceptable levels of profitability, even if collection rates are less than we currently forecast.

The following table presents forecasted Consumer Loan collection rates, advance rates, the spread (the forecasted collection rate less the advance rate), and the percentage of the forecasted collections that had been realized as of March 31, 2011. All amounts, unless otherwise noted, are presented as a percentage of the initial balance of the Consumer Loan (principal + interest). The table includes both Dealer Loans and Purchased Loans.

| Consumer Loan Assignment Year | As of March 31, 2011    |               |          |                            |
|-------------------------------|-------------------------|---------------|----------|----------------------------|
|                               | Forecasted Collection % | Advance % (1) | Spread % | % of Forecast Realized (2) |
| 2002                          | 70.5%                   | 42.2%         | 28.3%    | 99.4%                      |
| 2003                          | 73.7%                   | 43.4%         | 30.3%    | 99.3%                      |
| 2004                          | 73.0%                   | 44.0%         | 29.0%    | 99.0%                      |
| 2005                          | 73.7%                   | 46.9%         | 26.8%    | 98.7%                      |
| 2006                          | 70.2%                   | 46.6%         | 23.6%    | 97.6%                      |
| 2007                          | 68.0%                   | 46.5%         | 21.5%    | 93.5%                      |
| 2008                          | 70.0%                   | 44.6%         | 25.4%    | 82.6%                      |
| 2009                          | 78.6%                   | 43.9%         | 34.7%    | 65.4%                      |
| 2010                          | 75.4%                   | 44.7%         | 30.7%    | 28.8%                      |
| 2011                          | 73.0%                   | 44.9%         | 28.1%    | 3.3%                       |

(1) Represents advances paid to Dealer-Partners on Consumer Loans assigned under our Portfolio Program and one-time payments made to Dealer-Partners to purchase Consumer Loans assigned under our Purchase Program as a percentage of the contractual amounts of the Consumer Loans. Payments of Dealer Holdback and accelerated Dealer Holdback are not included.

(2) Presented as a percentage of total forecasted collections.

The risk of a material change in our forecasted collection rate declines as the Consumer Loans age. For 2007 and prior Consumer Loan assignments, the risk of a material forecast variance is modest, as we have currently realized in excess of 90% of the expected collections. Conversely, the forecasted collection rates for more recent Consumer Loan assignments are less certain as a significant portion of our forecast has not been realized.

The spread between the forecasted collection rate and the advance rate declined during the 2004 through 2007 period as we increased advance rates during this period in response to a more difficult competitive environment. During 2008 and 2009, the spread increased as the competitive environment improved, and we reduced advance rates. In addition, during 2009, the spread was positively impacted by better than expected Consumer Loan performance. During 2010 and 2011, the spread decreased as we increased advance rates during this period in an attempt to maximize the amount of economic profit we generate in response to an increase in the amount of capital

available to fund new Loans.

The following table presents forecasted Consumer Loan collection rates, advance rates, and the spread (the forecasted collection rate less the advance rate) as of March 31, 2011 for Dealer Loans and Purchased Loans separately. All amounts are presented as a percentage of the initial balance of the Consumer Loan (principal + interest).

|                 | Consumer Loan Assignment Year | Forecasted<br>Collection<br>% | Advance<br>% (1) | Spread % |
|-----------------|-------------------------------|-------------------------------|------------------|----------|
| Dealer loans    | 2007                          | 68.0%                         | 45.8%            | 22.2%    |
|                 | 2008                          | 70.6%                         | 43.3%            | 27.3%    |
|                 | 2009                          | 78.6%                         | 43.5%            | 35.1%    |
|                 | 2010                          | 75.4%                         | 44.4%            | 31.0%    |
|                 | 2011                          | 73.0%                         | 44.7%            | 28.3%    |
| Purchased loans | 2007                          | 68.1%                         | 49.1%            | 19.0%    |
|                 | 2008                          | 69.1%                         | 46.7%            | 22.4%    |
|                 | 2009                          | 78.5%                         | 45.4%            | 33.1%    |
|                 | 2010                          | 75.6%                         | 47.0%            | 28.6%    |
|                 | 2011                          | 72.9%                         | 47.9%            | 25.0%    |

(1) Represents advances paid to Dealer-Partners on Consumer Loans assigned under our Portfolio Program and one-time payments made to Dealer-Partners to purchase Consumer Loans assigned under our Purchase Program as a percentage of the contractual amounts of the Consumer Loans. Payments of Dealer Holdback and accelerated Dealer Holdback are not included.

The advance rates presented for each Consumer Loan assignment year change over time due to the impact of transfers between Dealer and Purchased Loans. Under our Portfolio Program, certain events may result in Dealer-Partners forfeiting their rights to Dealer Holdback. We transfer the Dealer-Partner's Consumer Loans from the Dealer Loan portfolio to the Purchased Loan portfolio in the period this forfeiture occurs.

Although the advance rate on Purchased Loans is higher as compared to the advance rate on Dealer Loans, Purchased Loans do not require us to pay Dealer Holdback.

#### Consumer Loan Volume

The following table summarizes changes in Consumer Loan assignment volume in each of the last five quarters as compared to the same period in the previous year:

| Three Months Ended | Year over Year Percent<br>Change |                      |
|--------------------|----------------------------------|----------------------|
|                    | Unit<br>Volume                   | Dollar<br>Volume (1) |
| March 31, 2010     | 11.2%                            | 21.6%                |
| June 30, 2010      | 22.7%                            | 42.2%                |
| September 30, 2010 | 26.9%                            | 51.5%                |
| December 31, 2010  | 37.7%                            | 66.9%                |
| March 31, 2011     | 36.7%                            | 59.3%                |

(1) Represents advances paid to Dealer-Partners on Consumer Loans assigned under our Portfolio Program and one-time payments made to Dealer-Partners to purchase Consumer Loans assigned under our Purchase

Program. Payments of Dealer Holdback and accelerated Dealer Holdback are not included.

Consumer Loan assignment volumes depend on a number of factors including (1) the overall demand for our product (2) the amount of capital available to fund new Loans and (3) our assessment of the volume that our infrastructure can support. Our pricing strategy is intended to maximize the amount of economic profit we generate, within the confines of capital and infrastructure constraints. Our success in renewing our debt facilities and securing additional financing during 2009 and 2010 positioned us to grow year over year unit volumes. During the last four months of 2009, the first quarter of 2010, and the fourth quarter of 2010, we increased advance rates, which had a positive impact on unit volumes. While the advance increases also reduced the return on capital we expect to earn on new assignments, we believe it is very likely the advance increases had a positive impact on economic profit. Unit volume for the one month ended April 30, 2011 increased by 26.6% as compared to the same period in 2010.

The following table summarizes the changes in Consumer Loan unit volume and active Dealer-Partners:

|  | For the Three Months Ended March 31, |        |          |
|--|--------------------------------------|--------|----------|
|  | 2011                                 | 2010   | % Change |
| Consumer Loan unit volume  | 53,183                               | 38,903 | 36.7%    |
| Active Dealer-Partners (1)   | 2,775                                | 2,346  | 18.3%    |
| Average volume per active Dealer-Partner                           | 19.2                                 | 16.6   | 15.7%    |
| Consumer Loan unit volume from Dealer-Partners active both periods | 41,556                               | 34,659 | 19.9%    |
| Dealer-Partners active both periods                                | 1,801                                | 1,801  | -        |
| Average volume per Dealer-Partners active both periods             | 23.1                                 | 19.2   | 19.9%    |
| Consumer Loan unit volume from new Dealer-Partners                 | 2,177                                | 1,741  | 25.0%    |
| New active Dealer-Partners (2)                                     | 321                                  | 216    | 48.6%    |
| Average volume per new active Dealer-Partners                      | 6.8                                  | 8.1    | -16.0%   |
| Attrition (3)  | -10.9%                               | -20.8% |          |

- (1) Active Dealer-Partners are Dealer-Partners who have received funding for at least one Loan during the period.
- (2) New active Dealer-Partners are Dealer-Partners who enrolled in our program and have received funding for their first Loan from us during the period.
- (3) Attrition is measured according to the following formula: decrease in Consumer Loan unit volume from Dealer-Partners who have received funding for at least one Loan during the comparable period of the prior year but did not receive funding for any Loans during the current period divided by prior year comparable period Consumer Loan unit volume.

Consumer Loans are assigned to us as either Dealer Loans through our Portfolio Program or Purchased Loans through our Purchase Program. The following table summarizes the portion of our Consumer Loan volume that was assigned to us as Dealer Loans:

|  | For the Three Months Ended March 31, |       |
|--|--------------------------------------|-------|
|  | 2011                                 | 2010  |
| New Dealer Loan unit volume as a percentage of total unit volume         | 92.9%                                | 90.9% |
| New Dealer Loan dollar volume as a percentage of total dollar volume (1) | 91.1%                                | 88.6% |

- (1) Represents advances paid to Dealer-Partners on Consumer Loans assigned under our Portfolio Program and one-time payments made to Dealer-Partners to purchase Consumer Loans assigned under our Purchase Program. Payments of Dealer Holdback and accelerated Dealer Holdback are not included.

For the three months ended March 31, 2011, new Dealer Loan unit and dollar volume as a percentage of total unit and dollar volume were generally consistent with the same period in 2010.

As of March 31, 2011 and December 31, 2010, the net Dealer Loans receivable balance was 82.1% and 79.5%, respectively, of the total net Loans receivable balance.



## Results of Operations

## Three Months Ended March 31, 2011 Compared to Three Months Ended March 31, 2010

The following is a discussion of our results of operations and income statement data on a consolidated basis.

(Dollars in thousands, except per share data)

|   | For the Three Months Ended March 31, |           |          |
|---|--------------------------------------|-----------|----------|
|   | 2011                                 | 2010      | % Change |
| <b>Revenue:</b>   |                                      |           |          |
| Finance charges   | \$ 106,503                           | \$ 89,663 | 18.8%    |
| Premiums earned   | 8,543                                | 7,704     | 10.9%    |
| Other income  | 8,466                                | 5,895     | 43.6%    |
| Total revenue   | 123,512                              | 103,262   | 19.6%    |
| <b>Costs and expenses:</b>  |                                      |           |          |
| Salaries and wages  | 16,071                               | 16,110    | -0.2%    |
| General and administrative  | 5,633                                | 6,542     | -13.9%   |
| Sales and marketing   | 6,409                                | 4,810     | 33.2%    |
| Provision for credit losses   | 8,916                                | 6,426     | 38.7%    |
| Interest  | 12,623                               | 11,705    | 7.8%     |
| Provision for claims  | 6,599                                | 5,212     | 26.6%    |
| Total costs and expenses  | 56,251                               | 50,805    | 10.7%    |
| Income from continuing operations before provision for income taxes | 67,261                               | 52,457    | 28.2%    |
| Provision for income taxes  | 24,070                               | 20,442    | 17.7%    |
| Income from continuing operations                                   | 43,191                               | 32,015    | 34.9%    |
| <b>Discontinued operations</b>                                      |                                      |           |          |
| Loss from discontinued United Kingdom operations                    | -                                    | (5)       | -100.0%  |
| Provision for income taxes  | -                                    | -         | 0.0%     |
| Loss from discontinued operations                                   | -                                    | (5)       | -100.0%  |
| Net income  | \$ 43,191                            | \$ 32,010 | 34.9%    |
| <b>Net income per share:</b>  |                                      |           |          |
| Basic   | \$ 1.59                              | \$ 1.03   |          |
| Diluted   | \$ 1.57                              | \$ 1.01   |          |
| <b>Income from continuing operations per share:</b>                 |                                      |           |          |
| Basic   | \$ 1.59                              | \$ 1.03   |          |
| Diluted   | \$ 1.57                              | \$ 1.01   |          |
| <b>Loss from discontinued operations per share:</b>                 |                                      |           |          |
| Basic   | \$ -                                 | \$ -      |          |
| Diluted   | \$ -                                 | \$ -      |          |
| <b>Weighted average shares outstanding:</b>                         |                                      |           |          |
| Basic   | 27,196                               | 31,042    |          |
| Diluted   | 27,489                               | 31,584    |          |





## Continuing Operations

## Three Months Ended March 31, 2011 Compared to Three Months Ended March 31, 2010

The following table highlights changes in income from continuing operations for the three months ended March 31, 2011, as compared to 2010:

| (In thousands)  | Change    |
|---|-----------|
| Income from continuing operations for the three months ended March 31, 2010 | \$ 32,015 |
| Increase in finance charges   | 16,840    |
| Increase in premiums earned   | 839       |
| Increase in other income  | 2,571     |
| Increase in operating expenses (1)  | (651)     |
| Increase in provision for credit losses                                     | (2,490)   |
| Increase in interest  | (918)     |
| Increase in provision for claims  | (1,387)   |
| Increase in provision for income taxes                                      | (3,628)   |
| Income from continuing operations for the three months ended March 31, 2011 | \$ 43,191 |

(1) Operating expenses consist of salaries and wages, general and administrative, and sales and marketing expenses.

Finance Charges. For the three months ended March 31, 2011, finance charges increased \$16.8 million, or 18.8%, as compared to the same period in 2010. The increase was primarily the result of an increase in the average net Loans receivable balance, as follows:

| (Dollars in thousands)               | For the Three Months Ended March 31, |              |            |
|--------------------------------------|--------------------------------------|--------------|------------|
|                                      | 2011                                 | 2010         | Change     |
| Average net Loans receivable balance | \$ 1,258,789                         | \$ 1,050,731 | \$ 208,058 |
| Average yield on our Loan portfolio  | 33.8%                                | 34.1%        | -0.3%      |

The following table summarizes the impact each component had on the overall increase in finance charges for the three months ended March 31, 2011:

| (In thousands)   | Year over<br>Year<br>Change<br>For the<br>Three<br>Months<br>Ended<br>March 31,<br>2011 |
|--|---|
| Impact on finance charges:                                     |   |
| Due to an increase in the average net Loans receivable balance | \$ 17,754   |
| Due to a decrease in the average yield                         | (914)   |
| Total increase in finance charges                              | \$ 16,840   |

The increase in the average net Loans receivable balance was primarily due to growth in new Loan volume throughout 2010 and the first quarter of 2011, which was a result of advance rate increases we made during the first and fourth

quarters of 2010. The average yield on our Loan portfolio for the three months ended March 31, 2011 decreased slightly compared with the same period in 2010 as the lower yields on new Loans were partially offset by improvements in forecasted collection rates throughout 2010.

**Premiums Earned.** For the three months ended March 31, 2011, premiums earned increased \$0.8 million, or 10.9%, as compared to the same period in 2010. The increase is primarily due to growth in the size of our reinsurance portfolio which resulted from growth in new Consumer Loan assignments throughout 2010 and the first quarter of 2011 that was partially offset by the termination of our arrangement with one of our third party insurers during the fourth quarter of 2009.

**Other Income.** For the three months ended March 31, 2011, other income increased \$2.6 million, or 43.6%, as compared to the same period in 2010. The increase is primarily due to an increase in Guaranteed Asset Protection (“GAP”) profit sharing income. Under our arrangement with our third party GAP provider, we receive annual profit sharing payments based on the performance of our GAP program and these payments are recognized as income in the period received. For the three months ended March 31, 2011, we received a GAP profit sharing payment of \$3.7 million compared to \$0.7 million for the same period in 2010.

Operating Expenses. For the three months ended March 31, 2011, operating expenses increased \$0.7 million, or 2.4%, as compared to the same period in 2010, primarily due to the following:

- An increase in sales and marketing expense of \$1.6 million, or 33.2%, primarily due to increased sales commissions resulting from our growth in Consumer Loan assignment volume and the expansion of our sales force.
- A decrease in general and administrative expense of \$0.9 million, or 13.9%, primarily due to decreased legal costs and a refund received in the current period from the successful appeal of a property tax assessment.

Provision for Credit Losses. For the three months ended March 31, 2011, the provision for credit losses increased \$2.5 million, or 38.7%, as compared to the same period in 2010. Under GAAP, when forecasted future cash flows decline relative to the cash flows expected at the time of assignment, a provision for credit losses is recorded immediately as a current period expense and a corresponding allowance for credit losses is established. For purposes of calculating the required allowance, Dealer Loans are grouped by Dealer-Partner and Purchased Loans are grouped by month of purchase. As a result, regardless of the overall performance of the portfolio of Consumer Loans, a provision can be required if any individual Loan pool performs worse than expected. Conversely, a previously recorded provision can be reversed if any previously impaired individual Loan pool experiences an improvement in performance.

During the three months ended March 31, 2011, overall Consumer Loan performance was generally consistent with our expectations at the start of the period. However, impaired Loan pools experienced net declines in forecasted cash flows, resulting in a provision for credit losses of \$8.9 million for the three months ended March 31, 2011, of which \$9.4 million related to Dealer Loans offset by a reversal of provision of \$0.5 million related to Purchased Loans. During the three months ended March 31, 2010, overall Consumer Loan performance exceeded our expectations at the start of the period. However, impaired Loan pools within our portfolio experienced net declines in forecasted cash flows, resulting in a provision for credit losses of \$6.4 million for the three months ended March 31, 2010, of which \$3.4 million related to Dealer Loans and \$3.0 million related to Purchased Loans.

Interest. For the three months ended March 31, 2011, interest expense increased \$0.9 million, or 7.8%, as compared to the same period in 2010. The following table shows interest expense, the average outstanding debt balance, and the pre-tax average cost of debt for the three months ended March 31, 2011 and 2010:

| (Dollars in thousands)           | For the Three Months<br>Ended March 31, |           |
|----------------------------------|---|-----------|
|                                  | 2011                                    | 2010      |
| Interest expense                 | \$ 12,623                               | \$ 11,705 |
| Average outstanding debt balance | 723,781                                 | 492,069   |
| Pre-tax average cost of debt     | 7.0%                                    | 9.5%      |

For the three months ended March 31, 2011, the increase in interest expense is primarily due to the increase in the average outstanding debt balance, partially offset by a decline in our pre-tax average cost of debt. The average outstanding debt balance increased compared to the same period in 2010 due to the use of the debt proceeds to fund stock repurchases and the growth in new Consumer Loan assignments. The decline in our pre-tax average cost of debt resulted from more favorable pricing on our revolving credit facilities and a decrease in available and unused credit capacity.

Provision for Claims. For the three months ended March 31, 2011, provision for claims increased \$1.4 million, or 26.6%, as compared to the same period in 2010. The increase was due to an increase in the size of our reinsurance portfolio and an increase in claims paid per reinsured vehicle service contract.

Provision for Income Taxes. For the three months ended March 31, 2011, the effective tax rate decreased to 35.8%, from 39.0% in the same period in 2010 primarily due to changes in the reserve for uncertain tax positions and related interest.

#### Liquidity and Capital Resources

We need capital to fund new Loans and pay Dealer Holdback. Our primary sources of capital are cash flows from operating activities, collections of Consumer Loans and borrowings under: (1) a revolving secured line of credit with a commercial bank syndicate; (2) revolving secured warehouse facilities with institutional investors; (3) Term ABS financings with qualified institutional investors; and (4) Senior Notes. There are various restrictive debt covenants for each financing arrangement and we are in compliance with those covenants as of March 31, 2011. For information regarding these financings and the covenants included in the related documents, see Note 5 to the consolidated financial statements contained in Item 1 of this Form 10-Q, which is incorporated herein by reference.

On March 3, 2011, we issued \$100.0 million aggregate principal amount of Senior Notes, which, together with the \$250.0 million aggregate principal amount of Senior Notes we issued on February 1 2010, are governed by an indenture, dated as of February 1, 2010, as amended and supplemented (the "Indenture"), among us, as the issuer; our subsidiaries Buyers Vehicle Protection Plan, Inc. and Vehicle Remarketing Services, Inc., as guarantors; and U.S. Bank National Association, as trustee. The Senior Notes issued during the first quarter of 2011 have the same terms as the previously issued Senior Notes, other than issue price and issue date, and all of the Senior Notes are treated as a single class under the Indenture.

The Senior Notes mature on February 1, 2017 and bear interest at a rate of 9.125% per annum, computed on the basis of a 360-day year comprised of twelve 30-day months and payable semi-annually on February 1 and August 1 of each year, beginning on August 1, 2010. The Senior Notes issued during the first quarter of 2011 were issued at a price of 106.0% of their aggregate principal amount, resulting in gross proceeds of \$106.0 million, and a yield to maturity of 7.83% per annum.

Cash and cash equivalents increased to \$4.6 million as of March 31, 2011 from \$3.8 million as of December 31, 2010. Our total balance sheet indebtedness increased to \$886.3 million as of March 31, 2011 from \$685.7 million as of December 31, 2010 primarily due to the completion of a tender offer to purchase \$125.0 million of our common stock using the proceeds from the issuance of \$100.0 million of Senior Notes and borrowing under our \$170.0 million revolving secured line of credit facility and the growth in new Consumer Loan assignments.

#### Contractual Obligations

A summary of our scheduled principal debt maturities as of March 31, 2011 is as follows:

(In thousands)

| Year              | Scheduled<br>Principal<br>Debt<br>Maturities<br>(1) |
|-------------------|---|
| Remainder of 2011 | \$ 54,515   |
| 2012              | 203,574   |
| 2013              | 161,994   |
| 2014              | 115,782   |
| 2015              | -   |
| Thereafter        | 350,000   |
| <b>Total</b>      | <b>\$ 885,865</b>                                   |

(1) The principal maturities of certain financings are estimated based on forecasted collections.

The amounts presented exclude the net unamortized debt premium of \$0.5 million.

Based upon anticipated cash flows, management believes that cash flows from operations and its various financing alternatives will provide sufficient financing for debt maturities and for future operations. Our ability to borrow funds may be impacted by economic and financial market conditions. If the various financing alternatives were to become limited or unavailable to us, our operations and liquidity could be materially and adversely affected.

### Critical Accounting Estimates

Our consolidated financial statements are prepared in accordance with GAAP. The preparation of these financial statements requires management to make estimates and judgments 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 revenues and expenses during the reporting period. On an ongoing basis, we review our accounting policies, assumptions, estimates and judgments to ensure that our financial statements are presented fairly and in accordance with GAAP. Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2010 discusses several critical accounting estimates, which we believe involve a high degree of judgment and complexity. There have been no material changes to the estimates and assumptions associated with these accounting estimates from those discussed in our Annual Report on Form 10-K for the year ended December 31, 2010.

### Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a material current or future effect on our financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

### Forward-Looking Statements

We make forward-looking statements in this report and may make such statements in future filings with the Securities and Exchange Commission ("SEC"). We may also make forward-looking statements in our press releases or other public or shareholder communications. Our forward-looking statements are subject to risks and uncertainties and include information about our expectations and possible or assumed future results of operations. When we use any of the words "may," "will," "should," "believe," "expect," "anticipate," "assume," "forecast," "estimate," "intend," "plan," or similar expressions, we are making forward-looking statements.

We claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995 for all of our forward-looking statements. These forward-looking statements represent our outlook only as of the date of this report. While we believe that our forward-looking statements are reasonable, actual results could differ materially since the statements are based on our current expectations, which are subject to risks and uncertainties. Factors that might cause such a difference include, but are not limited to, the factors set forth in Item 1A of our Form 10-K for the year ended December 31, 2010, other risk factors discussed herein or listed from time to time in our reports filed with the SEC and the following:

- Our inability to accurately forecast and estimate the amount and timing of future collections could have a material adverse effect on results of operations.
  - We may be unable to execute our business strategy due to current economic conditions.
- We may be unable to continue to access or renew funding sources and obtain capital needed to maintain and grow our business.
  - The terms of our debt limit how we conduct our business.
- A violation of the terms of our Term ABS facilities or revolving secured warehouse facilities could have a materially adverse impact on our operations.
- The conditions of the U.S. and international capital markets may adversely affect lenders with which we have relationships, causing us to incur additional costs and reducing our sources of liquidity, which may adversely affect our financial position, liquidity and results of operations.
- Our substantial debt could negatively impact our business, prevent us from satisfying our debt obligations and adversely affect our financial condition.
- Due to competition from traditional financing sources and non-traditional lenders, we may not be able to compete successfully.
- We may not be able to generate sufficient cash flows to service our outstanding debt and fund operations and may be forced to take other actions to satisfy our obligations under such debt.

- Interest rate fluctuations may adversely affect our borrowing costs, profitability and liquidity.
- Reduction in our credit rating could increase the cost of our funding from, and restrict our access to, the capital markets and adversely affect our liquidity, financial condition and results of operations.
- We may incur substantially more debt and other liabilities. This could exacerbate further the risks associated with our current debt levels.
- The regulation to which we are or may become subject could result in a material adverse effect on our business.
- Adverse changes in economic conditions, the automobile or finance industries, or the non-prime consumer market could adversely affect our financial position, liquidity and results of operations, the ability of key vendors that we depend on to supply us with services, and our ability to enter into future financing transactions.
- Litigation we are involved in from time to time may adversely affect our financial condition, results of operations and cash flows.
- Changes in tax laws and the resolution of uncertain income tax matters could have a material adverse effect on our results of operations and cash flows from operations.
- Our operations are dependent on technology.
- Reliance on third parties to administer our ancillary product offerings could adversely affect our business and financial results.



- We are dependent on our senior management and the loss of any of these individuals or an inability to hire additional team members could adversely affect our ability to operate profitably.
- Our reputation is a key asset to our business, and our business may be affected by how we are perceived in the marketplace.
  - The concentration of our Dealer-Partners in several states could adversely affect us.
- Failure to properly safeguard confidential consumer information could subject us to liability, decrease our profitability and damage our reputation.
  - Our founder controls a majority of our common stock, has the ability to control matters requiring shareholder approval and has interests which may conflict with the interests of our other security holders.
  - Reliance on our outsourced business functions could adversely affect our business.
- Natural disasters, acts of war, terrorist attacks and threats or the escalation of military activity in response to these attacks or otherwise may negatively affect our business, financial condition and results of operations.

Other factors not currently anticipated by management may also materially and adversely affect our results of operations. We do not undertake, and expressly disclaim any obligation, to update or alter our statements whether as a result of new information, future events or otherwise, except as required by applicable law.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Refer to our Annual Report on Form 10-K for the year ended December 31, 2010 for a complete discussion of our market risk. There have been no material changes to the market risk information included in our 2010 Annual Report on Form 10-K.

ITEM 4. CONTROLS AND PROCEDURES.

Evaluation of disclosure controls and procedures.

(a) Disclosure Controls and Procedures. Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this report. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, our disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by us in the reports that we file or submit under the Exchange Act and are effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

(b) Internal Control Over Financial Reporting. There have not been any changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II. - OTHER INFORMATION

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

## Stock Repurchases

In 1999, our board of directors approved a stock repurchase program which authorizes us to repurchase common shares in the open market or in privately negotiated transactions at price levels we deem attractive. As of March 31, 2011, we have authorization to repurchase up to \$29.1 million of our common stock under this program.

The following table summarizes stock repurchases for the three months ended March 31, 2011:

| Period                          | Total<br>Number of<br>Shares<br>Purchased | Average<br>Price Paid<br>per Share | Total<br>Number of<br>Shares<br>Purchased<br>as Part of<br>Publicly<br>Announced<br>Plans or<br>Programs | Maximum<br>Dollar<br>Value that<br>May Yet Be<br>Used to<br>Purchase<br>Shares<br>Under the<br>Plans or<br>Programs |
|---------------------------------|---|------------------------------------|--|---|
| January 1 to January 31, 2011   | -   | \$ -                               | -  | \$ 29,113,295   |
| February 1 to February 28, 2011 | 19,550*                                   | 70.380                             | -  | 29,113,295  |
| March 1 to March 31, 2011       | 1,904,761**                               | 65.625                             | 1,904,761  | 29,113,295  |
|                                 | 1,924,311                                 | \$ 65.673                          | 1,904,761  |   |

\*Amount represents shares of common stock released to us by team members as payment of tax withholdings due to us upon the vesting of restricted stock.

\*\*On February 9, 2011, we commenced a tender offer to repurchase up to 1,904,761 shares of our outstanding common stock at a price of \$65.625 per share. Upon expiration of the tender offer on March 10, 2011, we repurchased 1,904,761 common shares at a cost of approximately \$125.0 million.

## ITEM 6. EXHIBITS

See Index of Exhibits following the signature page, which is incorporated herein by reference.

SIGNATURE

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.

CREDIT ACCEPTANCE CORPORATION  
(Registrant)

By: /s/ Kenneth S. Booth  
Kenneth S. Booth  
Chief Financial Officer  
(Principal Financial Officer and Principal  
Accounting Officer)

Date: May 2, 2011

INDEX OF EXHIBITS

| Exhibit No. | Description  |
|-------------|--|
| 4(f)(144)   | 1 First Supplemental Indenture, dated as of March 3, 2011, among the Company, the Guarantors named therein and U.S. Bank National Association, as trustee.   |
| 4(f)(145)   | 1 Registration Rights Agreement, dated March 3, 2011, among Credit Acceptance Corporation, Buyers Vehicle Protection Plan, Inc., Vehicle Remarketing Services, Inc. and the representative of the initial purchasers of the Company's 9.125% First Priority Senior Secured Notes due 2017 issued on March 3, 2011. |
| 31(a)       | 2 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.  |
| 31(b)       | 2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.  |
| 32(a)       | 2 Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.   |
| 32(b)       | 2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.   |

1 Previously filed as an exhibit to the Company's Current Report on Form 8-K, dated March 3, 2011, and incorporated herein by reference.

2

Filed herewith.

