

ENCORE CAPITAL GROUP INC

Form 10-Q

November 09, 2016

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

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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 September 30, 2016

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: 000-26489

ENCORE CAPITAL GROUP, INC.

(Exact name of registrant as specified in its charter)

Delaware 48-1090909

(State or other jurisdiction of (IRS Employer  
incorporation or organization) Identification No.)

3111 Camino Del Rio North, Suite 103 92108

San Diego, California

(Address of principal executive offices) (Zip code)

(877) 445 - 4581

(Registrant's telephone number, including area code)

(Not Applicable)

(Former name, former address and former fiscal year, if changed since last report)

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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 last 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 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. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

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| Class                          | Outstanding at November 3, 2016 |
|--------------------------------|---------------------------------|
| Common Stock, \$0.01 par value | 25,532,227 shares               |

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## PART I – FINANCIAL INFORMATION

## Item 1—Condensed Consolidated Financial Statements (Unaudited)

## ENCORE CAPITAL GROUP, INC.

## Condensed Consolidated Statements of Financial Condition

(In Thousands, Except Par Value Amounts)

(Unaudited)

|  | September 30,<br>2016 | December 31,<br>2015 |
|--|-----------------------|----------------------|
| Assets   |                       |                      |
| Cash and cash equivalents  | \$ 157,672            | \$ 123,993           |
| Investment in receivable portfolios, net   | 2,397,831             | 2,440,669            |
| Property and equipment, net  | 66,703                | 72,546               |
| Deferred court costs, net  | 57,089                | 75,239               |
| Other assets   | 206,403               | 148,762              |
| Goodwill   | 819,785               | 924,847              |
| Assets associated with discontinued operations   | —                     | 388,763              |
| Total assets   | \$ 3,705,483          | \$ 4,174,819         |
| Liabilities and equity   |                       |                      |
| Liabilities:   |                       |                      |
| Accounts payable and accrued liabilities   | \$ 217,242            | \$ 290,608           |
| Debt   | 2,848,443             | 2,944,063            |
| Other liabilities  | 27,718                | 59,226               |
| Liabilities associated with discontinued operations  | —                     | 232,434              |
| Total liabilities  | 3,093,403             | 3,526,331            |
| Commitments and contingencies  |                       |                      |
| Redeemable noncontrolling interest   | 33,755                | 38,624               |
| Redeemable equity component of convertible senior notes  | 3,798                 | 6,126                |
| Equity:  |                       |                      |
| Convertible preferred stock, \$.01 par value, 5,000 shares authorized, no shares issued and outstanding  | —                     | —                    |
| Common stock, \$.01 par value, 50,000 shares authorized, 25,532 shares and 25,288 shares issued and outstanding as of September 30, 2016 and December 31, 2015, respectively | 255                   | 253                  |
| Additional paid-in capital   | 83,521                | 110,533              |
| Accumulated earnings   | 597,247               | 543,489              |
| Accumulated other comprehensive loss   | (103,320)             | (57,822)             |
| Total Encore Capital Group, Inc. stockholders' equity  | 577,703               | 596,453              |
| Noncontrolling interest  | (3,176)               | 7,285                |
| Total equity   | 574,527               | 603,738              |
| Total liabilities, redeemable equity and equity  | \$ 3,705,483          | \$ 4,174,819         |

The following table includes assets that can only be used to settle the liabilities of the Company's consolidated variable interest entities ("VIEs") and the creditors of the VIEs have no recourse to the Company. These assets and liabilities are included in the consolidated statements of financial condition above. See Note 11, "Variable Interest Entity" for additional information on the Company's VIE.

|  | September 30,<br>2016 | December 31,<br>2015 |
|--|-----------------------|----------------------|
| Assets                                   |                       |                      |
| Cash and cash equivalents                | \$ 55,158             | \$ 50,483            |
| Investment in receivable portfolios, net | 1,038,119             | 1,197,513            |

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|   |           |            |
|---|-----------|------------|
| Property and equipment, net   | 16,859    | 19,767     |
| Deferred court costs, net   | 20,836    | 33,296     |
| Other assets  | 58,146    | 31,679     |
| Goodwill  | 616,859   | 706,812    |
| Assets associated with discontinued operations                        | —         | 92,985     |
| <b>Liabilities</b>  |           |            |
| Accounts payable and accrued liabilities                              | \$ 89,056 | \$ 142,375 |
| Debt  | 1,591,403 | 1,665,009  |
| Other liabilities   | 770       | 839        |
| Liabilities associated with discontinued operations                   | —         | 58,923     |
| See accompanying notes to condensed consolidated financial statements |           |            |

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## ENCORE CAPITAL GROUP, INC.

## Condensed Consolidated Statements of Operations

(In Thousands, Except Per Share Amounts)

(Unaudited)

|   | Three Months Ended<br>September 30, |             | Nine Months Ended<br>September 30, |            |
|---|-------------------------------------|-------------|------------------------------------|------------|
|   | 2016                                | 2015        | 2016                               | 2015       |
| Revenues  |                                     |             |                                    |            |
| Revenue from receivable portfolios, net                                   | \$159,534                           | \$265,523   | \$697,080                          | \$799,934  |
| Other revenues  | 19,881                              | 13,391      | 60,794                             | 39,424     |
| Total revenues  | 179,415                             | 278,914     | 757,874                            | 839,358    |
| Operating expenses  |                                     |             |                                    |            |
| Salaries and employee benefits  | 67,783                              | 62,995      | 212,924                            | 194,116    |
| Cost of legal collections   | 56,932                              | 58,760      | 158,047                            | 170,834    |
| Other operating expenses  | 24,131                              | 22,217      | 75,420                             | 68,278     |
| Collection agency commissions   | 8,848                               | 9,381       | 28,242                             | 28,532     |
| General and administrative expenses                                       | 34,871                              | 86,789      | 103,044                            | 155,624    |
| Depreciation and amortization   | 8,032                               | 8,043       | 26,128                             | 24,058     |
| Total operating expenses  | 200,597                             | 248,185     | 603,805                            | 641,442    |
| (Loss) income from operations   | (21,182 )                           | 30,729      | 154,069                            | 197,916    |
| Other (expense) income  |                                     |             |                                    |            |
| Interest expense  | (48,632 )                           | (47,816 )   | (149,920 )                         | (136,369 ) |
| Other income (expense)  | 4,100                               | (924 )      | 14,358                             | 1,588      |
| Total other expense   | (44,532 )                           | (48,740 )   | (135,562 )                         | (134,781 ) |
| (Loss) income before income taxes   | (65,714 )                           | (18,011 )   | 18,507                             | 63,135     |
| Benefit (provision) for income taxes                                      | 13,768                              | 6,361       | (9,831 )                           | (23,174 )  |
| (Loss) income from continuing operations                                  | (51,946 )                           | (11,650 )   | 8,676                              | 39,961     |
| Income (loss) from discontinued operations, net of tax                    | —                                   | 2,286       | (3,182 )                           | 5,827      |
| Net (loss) income   | (51,946 )                           | (9,364 )    | 5,494                              | 45,788     |
| Net loss (income) attributable to noncontrolling interest                 | 50,422                              | (1,595 )    | 48,264                             | 335        |
| Net (loss) income attributable to Encore Capital Group, Inc. stockholders | \$(1,524 )                          | \$(10,959 ) | \$53,758                           | \$46,123   |
| Amounts attributable to Encore Capital Group, Inc.:                       |                                     |             |                                    |            |
| (Loss) income from continuing operations                                  | \$(1,524 )                          | \$(13,245 ) | \$56,940                           | \$40,296   |
| Income (loss) from discontinued operations, net of tax                    | —                                   | 2,286       | (3,182 )                           | 5,827      |
| Net (loss) income   | \$(1,524 )                          | \$(10,959 ) | \$53,758                           | \$46,123   |
| (Loss) earnings per share attributable to Encore Capital Group, Inc.:     |                                     |             |                                    |            |
| Basic (loss) earnings per share from:                                     |                                     |             |                                    |            |
| Continuing operations   | \$(0.06 )                           | \$(0.52 )   | \$2.22                             | \$1.56     |
| Discontinued operations   | \$—                                 | \$0.09      | \$(0.13 )                          | \$0.23     |
| Net basic (loss) earnings per share                                       | \$(0.06 )                           | \$(0.43 )   | \$2.09                             | \$1.79     |
| Diluted (loss) earnings per share from:                                   |                                     |             |                                    |            |
| Continuing operations   | \$(0.06 )                           | \$(0.52 )   | \$2.20                             | \$1.50     |
| Discontinued operations   | \$—                                 | \$0.09      | \$(0.12 )                          | \$0.21     |
| Net diluted (loss) earnings per share                                     | \$(0.06 )                           | \$(0.43 )   | \$2.08                             | \$1.71     |
| Weighted average shares outstanding:                                      |                                     |             |                                    |            |
| Basic   | 25,777                              | 25,450      | 25,690                             | 25,800     |

|         |        |        |        |        |
|---------|--------|--------|--------|--------|
| Diluted | 25,777 | 25,450 | 25,885 | 26,912 |
|---------|--------|--------|--------|--------|

See accompanying notes to condensed consolidated financial statements

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## ENCORE CAPITAL GROUP, INC.

Condensed Consolidated Statements of Comprehensive Income  
(Unaudited, In Thousands)

|   | Three Months Ended<br>September 30, |            | Nine Months<br>Ended<br>September 30, |          |
|---|-------------------------------------|------------|---------------------------------------|----------|
|   | 2016                                | 2015       | 2016                                  | 2015     |
| Net (loss) income   | \$(51,946)                          | \$(9,364)  | \$5,494                               | \$45,788 |
| Other comprehensive income (loss), net of tax:                                      |                                     |            |                                       |          |
| Change in unrealized gains/losses on derivative instruments:                        |                                     |            |                                       |          |
| Unrealized gain (loss) on derivative instruments                                    | 983                                 | (615)      | 487                                   | (26)     |
| Income tax effect   | (384)                               | 242        | (190)                                 | 2        |
| Unrealized gain (loss) on derivative instruments, net of tax                        | 599                                 | (373)      | 297                                   | (24)     |
| Change in foreign currency translation:   |                                     |            |                                       |          |
| Unrealized loss on foreign currency translation                                     | (11,456)                            | (13,995)   | (47,221)                              | (26,854) |
| Income tax effect   | 73                                  | (115)      | 1,426                                 | (1,479)  |
| Unrealized loss on foreign currency translation, net of tax                         | (11,383)                            | (14,110)   | (45,795)                              | (28,333) |
| Other comprehensive loss, net of tax  | (10,784)                            | (14,483)   | (45,498)                              | (28,357) |
| Comprehensive (loss) income   | (62,730)                            | (23,847)   | (40,004)                              | 17,431   |
| Comprehensive loss (income) attributable to noncontrolling interest:                |                                     |            |                                       |          |
| Net loss (income)   | 50,422                              | (1,595)    | 48,264                                | 335      |
| Unrealized loss (gain) on foreign currency translation                              | 115                                 | 2,308      | (807)                                 | 2,960    |
| Comprehensive loss attributable to noncontrolling interest                          | 50,537                              | 713        | 47,457                                | 3,295    |
| Comprehensive (loss) income attributable to Encore Capital Group, Inc. stockholders | \$(12,193)                          | \$(23,134) | \$7,453                               | \$20,726 |
| See accompanying notes to condensed consolidated financial statements               |                                     |            |                                       |          |



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ENCORE CAPITAL GROUP, INC.  
Condensed Consolidated Statements of Cash Flows  
(Unaudited, In Thousands)

|  | Nine Months Ended<br>September 30, |            |
|--|------------------------------------|------------|
|  | 2016                               | 2015       |
| Operating activities:  |                                    |            |
| Net income   | \$5,494                            | \$45,788   |
| Adjustments to reconcile net income to net cash provided by operating activities:        |                                    |            |
| Loss (income) from discontinued operations, net of income taxes                          | 1,352                              | (5,827 )   |
| Depreciation and amortization  | 26,128                             | 24,058     |
| Non-cash interest expense, net   | 28,557                             | 25,529     |
| Stock-based compensation expense   | 9,502                              | 17,259     |
| Gain on derivative instruments, net  | (10,885 )                          | —          |
| Deferred income taxes  | (46,524 )                          | (257 )     |
| Excess tax benefit from stock-based payment arrangements                                 | —                                  | (1,705 )   |
| Loss on sale of discontinued operations, net of tax                                      | 1,830                              | —          |
| Provision for (reversal of) allowances on receivable portfolios, net                     | 86,777                             | (3,958 )   |
| Changes in operating assets and liabilities  |                                    |            |
| Deferred court costs and other assets  | 7,572                              | (31,347 )  |
| Prepaid income tax and income taxes payable  | (2,485 )                           | (49,431 )  |
| Accounts payable, accrued liabilities and other liabilities                              | (24,146 )                          | 38,364     |
| Net cash provided by operating activities from continuing operations                     | 83,172                             | 58,473     |
| Net cash provided by operating activities from discontinued operations                   | 2,096                              | 4,908      |
| Net cash provided by operating activities  | 85,268                             | 63,381     |
| Investing activities:  |                                    |            |
| Cash paid for acquisitions, net of cash acquired   | (675 )                             | (236,214 ) |
| Proceeds from divestiture of business, net of cash divested                              | 106,041                            | —          |
| Purchases of receivable portfolios, net of put-backs                                     | (712,706 )                         | (549,957 ) |
| Collections applied to investment in receivable portfolios, net                          | 507,552                            | 488,174    |
| Purchases of property and equipment  | (16,548 )                          | (15,754 )  |
| Proceeds from derivative instruments, net  | 10,038                             | —          |
| Net cash used in investing activities from continuing operations                         | (106,298 )                         | (313,751 ) |
| Net cash provided by (used in) used in investing activities from discontinued operations | 14,685                             | (41,154 )  |
| Net cash used in investing activities  | (91,613 )                          | (354,905 ) |
| Financing activities:  |                                    |            |
| Payment of loan costs  | (3,750 )                           | (7,316 )   |
| Proceeds from credit facilities  | 455,786                            | 911,588    |
| Repayment of credit facilities   | (443,968 )                         | (471,610 ) |
| Repayment of senior secured notes  | (14,343 )                          | (11,250 )  |
| Repayment of securitized notes   | (935 )                             | (32,324 )  |
| Repurchase of common stock   | —                                  | (33,185 )  |
| Taxes paid related to net share settlement of equity awards                              | (4,113 )                           | (6,050 )   |
| Excess tax benefit from stock-based payment arrangements                                 | —                                  | 1,705      |
| Proceeds from other debt   | 35,080                             | —          |
| Other, net   | (10,070 )                          | (5,703 )   |
| Net cash provided by financing activities  | 13,687                             | 345,855    |
| Net increase in cash and cash equivalents  | 7,342                              | 54,331     |
| Effect of exchange rate changes on cash and cash equivalents                             | (3,263 )                           | (3,274 )   |

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|   |           |           |
|---|-----------|-----------|
| Cash and cash equivalents, beginning of period                        | 153,593   | 124,163   |
| Cash and cash equivalents, end of period                              | 157,672   | 175,220   |
| Cash and cash equivalents of discontinued operations, end of period   | —         | 31,825    |
| Cash and cash equivalents of continuing operations, end of period     | \$157,672 | \$143,395 |
| See accompanying notes to condensed consolidated financial statements |           |           |

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ENCORE CAPITAL GROUP, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

Note 1: Ownership, Description of Business, and Summary of Significant Accounting Policies

Encore Capital Group, Inc. (“Encore”), through its subsidiaries (collectively with Encore, the “Company”), is an international specialty finance company providing debt recovery solutions for consumers across a broad range of financial assets. The Company purchases portfolios of defaulted consumer receivables at deep discounts to face value and manages them by working with individuals as they repay their obligations and work toward financial recovery. Defaulted receivables are consumers’ unpaid financial commitments to credit originators, including banks, credit unions, consumer finance companies, commercial retailers, and telecommunication companies. Defaulted receivables may also include receivables subject to bankruptcy proceedings.

Financial Statement Preparation and Presentation

The accompanying interim condensed consolidated financial statements have been prepared by the Company, without audit, in accordance with the instructions to the Quarterly Report on Form 10-Q, and Rule 10-01 of Regulation S-X promulgated by the United States Securities and Exchange Commission (the “SEC”) and, therefore, do not include all information and footnotes necessary for a fair presentation of its consolidated financial position, results of operations and cash flows in accordance with accounting principles generally accepted in the United States (“GAAP”).

In the opinion of management, the unaudited financial information for the interim periods presented reflects all adjustments, consisting of only normal and recurring adjustments, necessary for a fair presentation of the Company’s consolidated financial position, results of operations, and cash flows. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2015. Operating results for interim periods are not necessarily indicative of operating results for an entire fiscal year.

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

Basis of Consolidation

The condensed consolidated financial statements have been prepared in conformity with GAAP, and reflect the accounts and operations of the Company and those of its subsidiaries in which the Company has a controlling financial interest. The Company also consolidates VIEs, for which it is the primary beneficiary. The primary beneficiary has both (a) the power to direct the activities of the VIE that most significantly affect the entity’s economic performance, and (b) either the obligation to absorb losses or the right to receive benefits. Refer to Note 11, “Variable Interest Entity,” for further details. All intercompany transactions and balances have been eliminated in consolidation.

Translation of Foreign Currencies

The financial statements of certain of the Company’s foreign subsidiaries are measured using their local currency as the functional currency. Assets and liabilities of foreign operations are translated into U.S. dollars using period-end exchange rates, and revenues and expenses are translated into U.S. dollars using average exchange rates in effect during each period. The resulting translation adjustments are recorded as a component of other comprehensive income or loss. Equity accounts are translated at historical rates, except for the change in retained earnings during the year which is the result of the income statement translation process. Intercompany transaction gains or losses at each period end arising from subsequent measurement of balances for which settlement is not planned or anticipated in the foreseeable future are included as translation adjustments and recorded within other comprehensive income or loss.

Transaction gains and losses are included in other income or expense.

Reclassifications

Certain immaterial reclassifications have been made to the condensed consolidated financial statements to conform to the current year’s presentation.

Recent Accounting Pronouncements

In August 2016, the Financial Accounting Standards Board (the “FASB”) issued Accounting Standards Update (“ASU”) 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (“ASU 2016-15”). The FASB issued ASU 2016-15 to decrease the diversity in practice in how certain cash receipts and cash

payments are presented and classified in the statement of cash flows. The amendments in this update provide guidance on eight specific cash

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flow issues. ASU 2016-15 is effective for reporting periods beginning after December 15, 2017, with early adoption permitted, provided that all of the amendments are adopted in the same period. The guidance requires application using a retrospective transition method. The Company is currently assessing the impact that adopting this guidance will have on its consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, “Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments” (“ASU 2016-13”). ASU 2016-13 applies a current expected credit loss model which is a new impairment model based on expected losses rather than incurred losses. Under this model, an entity would recognize an impairment allowance equal to its current estimate of all contractual cash flows that the entity does not expect to collect from financial assets measured at amortized cost. The estimate of expected credit losses should consider historical information, current information, as well as reasonable and supportable forecasts, including estimates of prepayments. The expected credit losses, and subsequent adjustments to such losses, will be recorded through an allowance account that is deducted from the amortized cost basis of the financial asset, with the net carrying value of the financial asset presented on the consolidated balance sheet at the amount expected to be collected. Most importantly, the standard eliminates the current accounting model for loans and debt securities acquired with deteriorated credit quality, which provides authoritative guidance for the accounting of the Company’s investment in receivable portfolios. Under this new standard, entities will gross up the initial amortized cost for the purchased financial assets with credit deterioration, the initial amortized cost will be the sum of (1) the purchase price and (2) the estimate of credit losses as of the date of acquisition. ASU 2016-13 is effective for reporting periods beginning after December 15, 2019 with early adoption permitted for reporting periods beginning after December 15, 2018. The Company is currently assessing the impact that adopting this guidance will have on its consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09, “Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting” (“ASU 2016-09”). ASU 2016-09 simplifies several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. For public entities, ASU 2016-09 is effective for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. Early adoption is permitted. The Company is currently assessing the impact that adopting this guidance will have on its consolidated financial statements.

In March 2016, the FASB issued ASU 2016-05, Derivatives and Hedging (Topic 815): Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships (“ASU 2016-05”) and ASU 2016-06, Derivatives and Hedging (Topic 815): Contingent Put and Call Options in Debt Instruments (“ASU 2016-06”). ASU 2016-05 clarifies that a change in the counterparty to a derivative instrument that has been designated as a hedging instrument does not, in and of itself, require dedesignation of that hedging relationship provided that all other hedge accounting criteria continue to be met. ASU 2016-06 clarifies the steps required to determine bifurcation of an embedded derivative. ASU 2016-05 and ASU 2016-06 are effective for fiscal years beginning after December 15, 2016, and interim periods within those years. Early adoption is permitted. The Company is currently assessing the impact that adopting this guidance will have on its consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842) (“ASU 2016-02”). ASU 2016-02 changes accounting for leases and requires lessees to recognize the assets and liabilities arising from all leases, including those classified as operating leases under previous accounting guidance, on the balance sheet and requires disclosure of key information about leasing arrangements to increase transparency and comparability among organizations. ASU 2016-02 is effective for the Company in its first quarter of fiscal 2019 on a modified retrospective basis and earlier adoption is permitted. The Company is currently assessing the impact that adopting this guidance will have on its consolidated financial statements.

### Change in Accounting Principle

In April 2015, the FASB issued ASU No. 2015-03, Interest—Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Cost (“ASU 2015-03”). ASU 2015-03 requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. ASU 2015-03 was effective beginning January 1, 2016, with early adoption

permitted. The update requires retrospective application and represents a change in accounting principle. The Company adopted ASU 2015-03 in the first quarter of 2016 and the retrospective application of this change in accounting principle on the consolidated balance sheet as of December 31, 2015 reclassified debt issuance costs of \$41.7 million, which were previously presented as other assets, as a reduction to the carrying value of the debt by the same amount. The adoption did not have an impact on the Company's condensed consolidated statements of operations or statements of cash flows in any period.

Note 2: Discontinued Operations

On March 31, 2016, the Company completed its previously announced divestiture of its membership interests in Propel Acquisition LLC (“Propel”) pursuant to the Securities Purchase Agreement (the “Purchase Agreement”), dated February 19,

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2016, among the Company and certain funds affiliated with Prophet Capital Asset Management LP. Pursuant to the Purchase Agreement, the application of the purchase price formula resulted in cash consideration paid to the Company at closing of \$144.4 million (net proceeds were \$106.0 million after divestiture of \$38.4 million in cash), subject to customary post-closing adjustments.

During the three months ended March 31, 2016, the Company recognized a loss of \$3.0 million related to the sale of Propel. Propel represented the Company's entire tax lien business reportable segment. Propel's operations are presented as discontinued operations in the Company's condensed consolidated statements of operations. Certain immaterial costs that may be eliminated as a result of the sale remained in continuing operations.

The following table presents the results of the discontinued operations during the periods presented (in thousands):

|   | Three Months Ended September 30, 2015 |           | Nine Months Ended September 30, 2016 |    | 2015     |         |
|---|---------------------------------------|-----------|--------------------------------------|----|----------|---------|
| Revenue   | \$                                    | -\$8,882  | \$4,950                              |    | \$24,457 |         |
| Salaries and employee benefits                                      |                                       | —(1,981 ) | (2,860 )                             |    | (6,153 ) |         |
| Other operating expenses  |                                       | —(1,736 ) | (1,473 )                             |    | (3,924 ) |         |
| General and administrative expenses                                 |                                       | —(1,213 ) | (1,551 )                             |    | (4,156 ) |         |
| Depreciation and amortization                                       |                                       | —(192 )   | (127 )                               |    | (611 )   |         |
| Income (loss) from discontinued operations, before income taxes     |                                       | —3,760    | (1,061 )                             |    | 9,613    |         |
| Loss on sale of discontinued operations, before income taxes        |                                       | —         | (3,000 )                             |    | —        |         |
| Total income (loss) on discontinued operations, before income taxes |                                       | —3,760    | (4,061 )                             |    | 9,613    |         |
| Income tax (provision) benefit                                      |                                       | —(1,474 ) | 879                                  |    | (3,786 ) |         |
| Total income (loss) from discontinued operations, net of tax        |                                       | \$        | -\$2,286                             | \$ | (3,182)  | \$5,827 |

## Note 3: Earnings (Loss) Per Share

Basic earnings or loss per share is calculated by dividing net earnings or loss attributable to Encore by the weighted average number of shares of common stock outstanding during the period. Diluted earnings per share is calculated on the basis of the weighted average number of shares of common stock plus the effect of dilutive potential common shares outstanding during the period using the treasury stock method. Dilutive potential common shares include outstanding stock options, restricted stock, and the dilutive effect of the convertible senior notes. In computing the diluted net loss per share for the three months ended September 30, 2016 and 2015, dilutive potential common shares are excluded from the diluted loss per share calculation because of their anti-dilutive effect.

A reconciliation of shares used in calculating earnings per basic and diluted shares follows (in thousands):

|  | Three Months Ended September 30, 2016 |        | Nine Months Ended September 30, 2016 |        | 2015 |  |
|--|---------------------------------------|--------|--------------------------------------|--------|------|--|
| Weighted average common shares outstanding—basic   | 25,777                                | 25,450 | 25,690                               | 25,800 |      |  |
| Dilutive effect of stock-based awards              | —                                     | —      | 195                                  | 265    |      |  |
| Dilutive effect of convertible senior notes        | —                                     | —      | —                                    | 847    |      |  |
| Weighted average common shares outstanding—diluted | 25,777                                | 25,450 | 25,885                               | 26,912 |      |  |

Anti-dilutive employee stock options outstanding were zero or negligible during the periods presented above.

## Note 4: Business Combinations

## dlc Acquisition

On June 1, 2015, Encore's U.K.-based subsidiary Cabot Credit Management Limited and its subsidiaries (collectively, "Cabot") acquired Hillesden Securities Ltd and its subsidiaries ("dlc"), a U.K.-based acquirer and collector of non-performing unsecured consumer debt for approximately £180.6 million (approximately \$274.7 million), (the "dlc

Acquisition”).

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The dlc Acquisition was accounted for using the acquisition method of accounting and, accordingly, the tangible and intangible assets acquired and liabilities assumed were recorded at their estimated fair values as of the date of the acquisition. Fair value measurements have been applied based on assumptions that market participants would use in the pricing of the respective assets and liabilities.

The components of the purchase price allocation for the dlc Acquisition were as follows (in thousands):

Purchase price:

|                          |           |
|--------------------------|-----------|
| Cash paid at acquisition | \$268,391 |
| Deferred consideration   | 6,306     |
| Total purchase price     | \$274,697 |

Allocation of purchase price:

|                                     |           |
|-------------------------------------|-----------|
| Cash                                | \$30,518  |
| Investment in receivable portfolios | 215,988   |
| Deferred court costs                | 760       |
| Property and equipment              | 1,327     |
| Other assets                        | 2,384     |
| Liabilities assumed                 | (46,435 ) |
| Identifiable intangible assets      | 3,669     |
| Goodwill                            | 66,486    |
| Total net assets acquired           | \$274,697 |

The goodwill recognized is primarily attributable to synergies that are expected to be achieved by combining dlc and Cabot's existing contingent collections operations. The entire goodwill of \$66.5 million related to the dlc Acquisition is not deductible for income tax purposes.

Other Acquisitions

In addition to the dlc Acquisition discussed above, the Company, through its subsidiaries, completed certain other acquisitions in 2016 and 2015. These acquisitions were immaterial to the Company's financial statements individually and in the aggregate.

Refer to Note 2, "Business Combinations" as disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2015, for a complete description of the Company's acquisition activities in 2015.

Note 5: Fair Value Measurements

The authoritative guidance for fair value measurements defines fair value as the price that would be received upon sale of an asset or the price paid to transfer a liability, in an orderly transaction between market participants at the measurement date (i.e., the "exit price"). The guidance utilizes a fair value hierarchy that prioritizes the inputs used in valuation techniques to measure fair value into three broad levels. The following is a brief description of each level:

Level 1: Observable inputs such as quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets or liabilities in active markets and quoted prices for identical or similar assets or liabilities in markets that are not active.

Level 3: Unobservable inputs, including inputs that reflect the reporting entity's own assumptions.

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## Financial Instruments Required To Be Carried At Fair Value

Financial assets and liabilities measured at fair value on a recurring basis are summarized below (in thousands):

|                                     | Fair Value Measurements as<br>of<br>September 30, 2016 |         |          |          |
|-------------------------------------|--|---------|----------|----------|
|                                     | Level 1  | Level 2 | Level 3  | Total    |
| Assets                              |  |         |          |          |
| Foreign currency exchange contracts | \$—  | \$1,466 | \$—      | \$1,466  |
| Liabilities                         |  |         |          |          |
| Foreign currency exchange contracts | —  | (72)    | —        | (72)     |
| Interest rate swap agreements       | —  | (199)   | —        | (199)    |
| Temporary Equity                    |  |         |          |          |
| Redeemable noncontrolling interests | —  | —       | (33,755) | (33,755) |

|                                     | Fair Value Measurements<br>as of<br>December 31, 2015 |         |          |          |
|-------------------------------------|---|---------|----------|----------|
|                                     | Level 1   | Level 2 | Level 3  | Total    |
| Assets                              |   |         |          |          |
| Foreign currency exchange contracts | \$—   | \$718   | \$—      | \$718    |
| Liabilities                         |   |         |          |          |
| Foreign currency exchange contracts | —   | (601)   | —        | (601)    |
| Interest rate swap agreements       | —   | (352)   | —        | (352)    |
| Temporary Equity                    |   |         |          |          |
| Redeemable noncontrolling interests | —   | —       | (38,624) | (38,624) |

## Assets

Foreign currency exchange contracts \$— \$718 \$— \$718

## Liabilities

Foreign currency exchange contracts —(601) — (601)

Interest rate swap agreements —(352) — (352)

## Temporary Equity

Redeemable noncontrolling interests — (38,624) (38,624)

## Derivative Contracts:

The Company uses derivative instruments to manage its exposure to fluctuations in interest rates and foreign currency exchange rates. Fair values of these derivative instruments are estimated using industry standard valuation models. These models project future cash flows and discount the future amounts to a present value using market-based observable inputs, including interest rate curves, foreign currency exchange rates, and forward and spot prices for currencies.

## Redeemable Noncontrolling Interests:

Some minority shareholders in certain subsidiaries of the Company have the right, at certain times, to require the Company to acquire their ownership interest in those entities at fair value and, in some cases, to force a sale of the subsidiary if the Company chooses not to purchase their interests at fair value. The noncontrolling interests subject to these arrangements are included in temporary equity as redeemable noncontrolling interests, and are adjusted to their estimated redemption amounts each reporting period with a corresponding adjustment to additional paid-in capital. Future reductions in the carrying amounts are subject to a “floor” amount that is equal to the fair value of the redeemable noncontrolling interests at the time they were originally recorded. The recorded value of the redeemable noncontrolling interests cannot go below the floor level. These adjustments do not affect the calculation of earnings per share.

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The components of the change in the redeemable noncontrolling interests for the periods ended September 30, 2016 and December 31, 2015 are presented in the following table (in thousands):

|  | Amount    |
|--|-----------|
| Balance at December 31, 2014   | \$28,885  |
| Addition to redeemable noncontrolling interest   | 9,409     |
| Net income attributable to redeemable noncontrolling interests                             | 1,371     |
| Adjustment of the redeemable noncontrolling interests to fair value                        | 2,349     |
| Effect of foreign currency translation attributable to redeemable noncontrolling interests | (3,390 )  |
| Balance at December 31, 2015   | 38,624    |
| Addition to redeemable noncontrolling interest   | 498       |
| Net loss attributable to redeemable noncontrolling interests                               | (37,029 ) |
| Adjustment of the redeemable noncontrolling interests to fair value                        | 32,470    |
| Effect of foreign currency translation attributable to redeemable noncontrolling interests | (808 )    |
| Balance at September 30, 2016  | \$33,755  |

**Financial Instruments Not Required To Be Carried At Fair Value****Investment in Receivable Portfolios:**

The Company records its investment in receivable portfolios at cost, which represents a significant discount from the contractual receivable balances due. The Company computes the fair value of its investment in receivable portfolios using Level 3 inputs by discounting the estimated future cash flows generated by its proprietary forecasting models. The key inputs include the estimated future gross cash flow, average cost to collect, and discount rate. In accordance with authoritative guidance related to fair value measurements, the Company estimates the average cost to collect and discount rates based on its estimate of what a market participant might use in valuing these portfolios. The determination of such inputs requires significant judgment, including assessing the assumed market participant's cost structure, its determination of whether to include fixed costs in its valuation, its collection strategies, and determining the appropriate weighted average cost of capital. The Company evaluates the use of these key inputs on an ongoing basis and refines the data as it continues to obtain better information from market participants in the debt recovery and purchasing business.

In the Company's current analysis, the estimated blended market participant cost to collect and discount rate is approximately 50.3% and 10.5%, respectively, for U.S. portfolios, approximately 29.9% and 11.9%, respectively, for Europe portfolios and approximately 32.9% and 11.0%, respectively for other geographies. Using this method, the fair value of investment in receivable portfolios was approximately \$2,165.0 million and \$2,473.8 million as of September 30, 2016 and December 31, 2015, respectively, as compared to the carrying value of \$2,397.83 million and \$2,440.67 million as of September 30, 2016 and December 31, 2015, respectively. A 100 basis point fluctuation in the cost to collect and discount rate used would result in an increase or decrease in the fair value of U.S. and European portfolios by approximately \$44.3 million and \$58.6 million, respectively, as of September 30, 2016. This fair value calculation does not represent, and should not be construed to represent, the underlying value of the Company or the amount that could be realized if its investment in receivable portfolios were sold.

**Deferred Court Costs:**

The Company capitalizes deferred court costs and provides a reserve for those costs that it believes will ultimately be uncollectible. The carrying value of net deferred court costs approximates fair value.

**Debt:**

The majority of Encore and its subsidiaries' borrowings are carried at historical amounts, adjusted for additional borrowings less principal repayments, which approximate fair value. These borrowings include Encore's senior secured notes and borrowings under its revolving credit and term loan facilities, Cabot's senior secured notes and borrowings under its revolving credit facility, and other borrowing under revolving credit facilities at certain of the Company's subsidiaries.

Encore's convertible senior notes are carried at historical cost, adjusted for the debt discount. The carrying value of the convertible senior notes was \$414.0 million and \$406.6 million as of September 30, 2016 and December 31, 2015, respectively. The fair value estimate for these convertible senior notes, which incorporates quoted market prices using

Level 2 inputs, was approximately \$382.8 million and \$372.2 million as of September 30, 2016 and December 31, 2015, respectively.

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Cabot's senior secured notes are carried at historical cost, adjusted for debt discount and debt premium. The carrying value of Cabot's senior secured notes was \$1.3 billion and \$1.4 billion, as of September 30, 2016 and December 31, 2015, respectively. The fair value estimate for these senior notes, which incorporates quoted market prices using Level 2 inputs, was \$1.3 billion and \$1.4 billion as of September 30, 2016 and December 31, 2015, respectively.

The Company's preferred equity certificates are legal obligations to the noncontrolling shareholders of certain subsidiaries. They are carried at the face amount, plus any accrued interest. The Company determined that the carrying value of these preferred equity certificates approximated fair value as of September 30, 2016 and December 31, 2015.

**Note 6: Derivatives and Hedging Instruments**

The Company may periodically enter into derivative financial instruments to manage risks related to interest rates and foreign currency. Certain of the Company's derivative financial instruments qualify for hedge accounting treatment under the authoritative guidance for derivatives and hedging.

The following table summarizes the fair value of derivative instruments as recorded in the Company's condensed consolidated statements of financial condition (in thousands):

|   | September 30, 2016     |            | December 31, 2015      |            |
|---|------------------------|------------|------------------------|------------|
|   | Balance Sheet Location | Fair Value | Balance Sheet Location | Fair Value |
| <b>Derivatives designated as hedging instruments:</b>     |                        |            |                        |            |
| Foreign currency exchange contracts                       | Other assets           | \$ 676     | Other assets           | \$ 718     |
| Foreign currency exchange contracts                       | Other liabilities      | (72 )      | Other liabilities      | (601 )     |
| <b>Derivatives not designated as hedging instruments:</b> |                        |            |                        |            |
| Foreign currency exchange contracts                       | Other assets           | 790        | Other assets           | —          |
| Interest rate swap agreements                             | Other liabilities      | (199 )     | Other liabilities      | (352 )     |

The Company has operations in foreign countries, which expose the Company to foreign currency exchange rate fluctuations due to transactions denominated in foreign currencies. To mitigate a portion of this risk, the Company enters into derivative financial instruments, principally foreign currency forward contracts with financial counterparties. The Company adjusts the level and use of derivatives as soon as practicable after learning that an exposure has changed and reviews all exposures and derivative positions on an ongoing basis.

**Derivatives Designated as Hedging Instruments**

Certain of the foreign currency forward contracts are designated as cash flow hedging instruments and qualify for hedge accounting treatment. Gains and losses arising from the effective portion of such contracts are recorded as a component of accumulated other comprehensive income ("OCI") as gains and losses on derivative instruments, net of income taxes. The hedging gains and losses in OCI are subsequently reclassified into earnings in the same period in which the underlying transactions affect the Company's earnings. If all or a portion of the forecasted transaction is cancelled, this would render all or a portion of the cash flow hedge ineffective and the Company would reclassify the ineffective portion of the hedge into earnings. The Company generally does not experience ineffectiveness of the hedge relationship and the accompanying consolidated financial statements do not include any such gains or losses. As of September 30, 2016, the total notional amount of the forward contracts that are designated as cash flow hedging instruments was \$33.6 million. All of these outstanding contracts qualified for hedge accounting treatment. The Company estimates that approximately \$0.2 million of net derivative gain included in OCI will be reclassified into earnings within the next 12 months. No gains or losses were reclassified from OCI into earnings as a result of forecasted transactions that failed to occur during the nine months ended September 30, 2016 and 2015.

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The following table summarizes the effects of derivatives in cash flow hedging relationships designated as hedging instruments on the Company's condensed consolidated statements of operations for the three and nine months ended September 30, 2016 and 2015 (in thousands):

| Derivatives Designated as Hedging Instruments | Gain or (Loss) Recognized in OCI - Effective Portion |                                  | Location of Gain or (Loss) Reclassified from OCI into Income - Effective Portion | Gain or (Loss) Reclassified from OCI into Income - Effective Portion |                                  | Location of Gain or (Loss) Recognized - Ineffective Portion and Amount Excluded from Effectiveness Testing | Amount of Gain or (Loss) Recognized - Ineffective Portion and Amount Excluded from Effectiveness Testing |                                  |
|---|--|----------------------------------|--|--|----------------------------------|--|--|----------------------------------|
|   | Three Months Ended September 30,                     | Three Months Ended September 30, |  | Three Months Ended September 30,                                     | Three Months Ended September 30, |  | Three Months Ended September 30,   | Three Months Ended September 30, |
|   | 2016   | 2015                             |  | 2016   | 2015                             |  | 2016   | 2015                             |
| Foreign currency exchange contracts           | \$ 989   | \$ (670 )                        | Salaries and employee benefits   | \$ 151   | \$ (153)                         | Other (expense) income   | \$ —   | \$ —                             |
| Foreign currency exchange contracts           | 171  | (126 )                           | General and administrative expenses  | 26   | (28 )                            | Other (expense) income   | —  | —                                |
| Derivatives Designated as Hedging Instruments | Gain or (Loss) Recognized in OCI - Effective Portion |                                  | Location of Gain or (Loss) Reclassified from OCI into Income - Effective Portion | Gain or (Loss) Reclassified from OCI into Income - Effective Portion |                                  | Location of Gain or (Loss) Recognized - Ineffective Portion and Amount Excluded from Effectiveness Testing | Amount of Gain or (Loss) Recognized - Ineffective Portion and Amount Excluded from Effectiveness Testing |                                  |
|   | Nine Months Ended September 30,                      | Nine Months Ended September 30,  |  | Nine Months Ended September 30,                                      | Nine Months Ended September 30,  |  | Nine Months Ended September 30,  | Nine Months Ended September 30,  |
|   | 2016   | 2015                             |  | 2016   | 2015                             |  | 2016   | 2015                             |
| Foreign currency exchange contracts           | \$ 1,284   | \$ (593 )                        | Salaries and employee benefits   | \$ 683   | \$ (468)                         | Other (expense) income   | \$ —   | \$ —                             |
| Foreign currency exchange contracts           | (19 )  | 24                               | General and administrative expenses  | 95   | (75 )                            | Other (expense) income   | —  | —                                |

## Derivatives Not Designated as Hedging Instruments

In 2016, Encore and its Cabot subsidiary collectively began entering into currency exchange forward contracts to reduce the effects of currency exchange rate fluctuations between the British Pound and Euro. These derivative contracts generally mature within one to three months and are not designated as hedge instruments for accounting

purposes. The Company continues to monitor the level of exposure of the foreign currency exchange risk and may enter into additional short-term forward contracts on an ongoing basis. The gains or losses on these derivative contracts are recognized in other income or expense based on the changes in fair value. Before the effect of income tax and noncontrolling interest, the net gain on these derivative contracts recognized in the Company's condensed consolidated statements of operations was \$3.3 million and \$10.7 million during the three and nine months ended September 30, 2016, respectively.

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The following table summarizes the effects of derivatives in cash flow hedging relationships not designated as hedging instruments on the Company's condensed consolidated statements of operations for the three and nine months ended September 30, 2016 and 2015 (in thousands):

| Derivatives Not Designated as Hedging Instruments  | Location of Gain or (Loss) Recognized in income on Derivative | Amount of Gain or (Loss) Recognized in Income on Derivative |      |                                      |      |
|--|---|---|------|--------------------------------------|------|
|  |   | Three Months Ended September 30, 2016                       | 2015 | Nine Months Ended September 30, 2016 | 2015 |
| Foreign currency exchange contracts <sup>(1)</sup> | Other income (expense)  | \$3,330   | \$   | -\$10,706                            | \$   |
| Interest rate swap agreements                      | Interest expense  | 39  | —    | 83                                   | —    |

After the effect of income tax and noncontrolling interest, the net impact of the derivative contracts to consolidated (1) net income from continuing operations attributable to Encore was a gain of \$0.5 million and \$2.1 million during the three and nine months ended September 30, 2016, respectively.

Note 7: Investment in Receivable Portfolios, Net

In accordance with the authoritative guidance for loans and debt securities acquired with deteriorated credit quality, discrete receivable portfolio purchases during the same fiscal quarter are aggregated into pools based on common risk characteristics. Common risk characteristics include risk ratings (e.g. FICO or similar scores), financial asset type, collateral type, size, interest rate, date of origination, term, and geographic location. The Company's static pools are typically grouped into credit card and telecom, purchased consumer bankruptcy, and mortgage portfolios. The Company further groups these static pools by geographic region or location. Portfolios acquired in business combinations are also grouped into these pools. During any fiscal quarter in which the Company has an acquisition of an entity that has portfolio, the entire historical portfolio of the acquired company is aggregated into the pool groups for that quarter, based on common characteristics, resulting in pools for that quarter that may consist of several different vintages of portfolio. Once a static pool is established, the portfolios are permanently assigned to the pool. The discount (i.e., the difference between the cost of each static pool and the related aggregate contractual receivable balance) is not recorded because the Company expects to collect a relatively small percentage of each static pool's contractual receivable balance. As a result, receivable portfolios are recorded at cost at the time of acquisition. The purchase cost of the portfolios includes certain fees paid to third parties incurred in connection with the direct acquisition of the receivable portfolios.

In compliance with the authoritative guidance, the Company accounts for its investments in receivable portfolios using either the interest method or the cost recovery method. The interest method applies an internal rate of return ("IRR") to the cost basis of the pool, which remains unchanged throughout the life of the pool, unless there is an increase in subsequent expected cash flows. Subsequent increases in expected cash flows are recognized prospectively through an upward adjustment of the pool's IRR over its remaining life. Subsequent decreases in expected cash flows do not change the IRR, but are recognized as an allowance to the cost basis of the pool, and are reflected in the consolidated statements of operations as a reduction in revenue, with a corresponding valuation allowance, offsetting the investment in receivable portfolios in the consolidated statements of financial condition. With gross collections being discounted at monthly IRRs, when collections are lower in the near term, even if substantially higher collections are expected later in the collection curve, an allowance charge could result.

The Company utilizes its proprietary forecasting models to continuously evaluate the economic life of each pool. During the quarter ended September 30, 2016, the Company revised the forecasting methodology it uses to value and calculate IRRs on certain portfolios in Europe by extending the collection forecast from 120 months to 180 months. This change was made as a result of (1) the Company having observed that older portfolios in Europe have consistently experienced cash collections beyond 120 months, (2) an expectation that regulatory changes in the United



Kingdom resulting in a reduction in the number of highly discounted near term one-time settlements, an increase in the number of payment plans, and an increase in the length of existing payment plans will cause a lengthening of the collections curve, (3) an expectation that, as a result of a higher percentage of semi-performing account purchases in the United Kingdom in recent years, newer vintages will have a larger percentage of collections after 120 months and (4) the Company's increased confidence in its ability to forecast future cash collections to 180 months. The increase in the collection forecast from 120 months to 180 months was applied effective July 1, 2016 to certain portfolios in Europe for which the Company could accurately forecast through such term. In addition, during the three months ended September 30, 2016, the Company recorded allowance charges of approximately \$94.0 million resulting from delays or shortfalls in near term collections against the forecasts for certain pools in Europe. These changes in forecasted future cash flows resulted in an increase in the aggregate total estimated remaining collections for the receivable portfolios of approximately \$296.5 million as of September 30, 2016. The increase in the collection forecast from 120 months to 180 months had the effect of reducing the allowance charges by approximately \$13.2 million. For portfolios in Europe that

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were not extended to 180 months, the Company will continue to include collection forecasts to 120 months in calculating accretion revenue and in its estimated remaining collection disclosures. In the United States, the Company will continue to include collection forecasts to 120 months in calculating accretion revenue. Expected collections beyond the 120 month collection forecast in the United States are included in its estimated remaining collection disclosures but are not included in the calculation of accretion revenue.

The Company accounts for each static pool as a unit for the economic life of the pool (similar to one loan) for recognition of revenue from receivable portfolios, for collections applied to the cost basis of receivable portfolios, and for provision for loss or allowance. Revenue from receivable portfolios is accrued based on each pool's IRR applied to each pool's adjusted cost basis. The cost basis of each pool is increased by revenue earned and portfolio allowance reversals and decreased by gross collections and portfolio allowances.

If the amount and timing of future cash collections on a pool of receivables are not reasonably estimable, the Company accounts for such portfolios on the cost recovery method as Cost Recovery Portfolios. The accounts in these portfolios have different risk characteristics than those included in other portfolios acquired during the same quarter, or the necessary information was not available to estimate future cash flows and, accordingly, they were not aggregated with other portfolios. Under the cost recovery method of accounting, no revenue is recognized until the purchase price of a Cost Recovery Portfolio has been fully recovered.

Accretable yield represents the amount of revenue the Company expects to generate over the remaining life of its existing investment in receivable portfolios based on estimated future cash flows. Total accretable yield is the difference between future estimated collections and the current carrying value of a portfolio. All estimated cash flows on portfolios where the cost basis has been fully recovered are classified as zero basis cash flows.

The following table summarizes the Company's accretable yield and an estimate of zero basis future cash flows at the beginning and end of the period presented (in thousands):

|  | Accretable<br>Yield | Estimate of<br>Zero Basis<br>Cash Flows | Total       |
|--|---------------------|---|-------------|
| December 31, 2015                      | \$3,047,640         | \$223,031                               | \$3,270,671 |
| Revenue recognized, net                | (238,547 )          | (31,547 )                               | (270,094 )  |
| Net additions on existing portfolios   | 39,538              | 8,071                                   | 47,609      |
| Additions for current purchases, net   | 193,654             | —                                       | 193,654     |
| Effect of foreign currency translation | (64,330 )           | 470                                     | (63,860 )   |
| Balance at March 31, 2016              | 2,977,955           | 200,025                                 | 3,177,980   |
| Revenue recognized, net                | (233,714 )          | (33,738 )                               | (267,452 )  |
| Net additions on existing portfolios   | 59,459              | 95,135                                  | 154,594     |
| Additions for current purchases, net   | 183,217             | —                                       | 183,217     |
| Effect of foreign currency translation | (181,223 )          | 245                                     | (180,978 )  |
| Balance at June 30, 2016               | 2,805,694           | 261,667                                 | 3,067,361   |
| Revenue recognized, net                | (119,543 )          | (39,991 )                               | (159,534 )  |
| Net additions on existing portfolios   | 299,212             | 22,862                                  | 322,074     |
| Additions for current purchases, net   | 180,079             | —                                       | 180,079     |
| Effect of foreign currency translation | (75,402 )           | 135                                     | (75,267 )   |
| Balance at September 30, 2016          | \$3,090,040         | \$244,673                               | \$3,334,713 |

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|  | Accretable<br>Yield | Estimate of<br>Zero Basis<br>Cash Flows | Total       |
|--|---------------------|---|-------------|
| Balance at December 31, 2014           | \$2,993,321         | \$66,392                                | \$3,059,713 |
| Revenue recognized, net                | (248,539 )          | (15,571 )                               | (264,110 )  |
| Net additions on existing portfolios   | 228,560             | 39,661                                  | 268,221     |
| Additions for current purchases, net   | 85,907              | —                                       | 85,907      |
| Effect of foreign currency translation | (108,046 )          | (54 )                                   | (108,100 )  |
| Balance at March 31, 2015              | 2,951,203           | 90,428                                  | 3,041,631   |
| Revenue recognized, net                | (243,425 )          | (26,876 )                               | (270,301 )  |
| Net additions on existing portfolios   | (40,337 )           | 74,587                                  | 34,250      |
| Additions for current purchases, net   | 395,009             | —                                       | 395,009     |
| Effect of foreign currency translation | 131,654             | (1 )                                    | 131,653     |
| Balance at June 30, 2015               | 3,194,104           | 138,138                                 | 3,332,242   |
| Revenue recognized, net                | (233,680 )          | (31,843 )                               | (265,523 )  |
| Net additions on existing portfolios   | 117,399             | 119,127                                 | 236,526     |
| Additions for current purchases, net   | 149,278             | —                                       | 149,278     |
| Effect of foreign currency translation | (120,970 )          | (1,209 )                                | (122,179 )  |
| Balance at September 30, 2015          | \$3,106,131         | \$224,213                               | \$3,330,344 |

During the three months ended September 30, 2016, the Company purchased receivable portfolios with a face value of \$1.5 billion for \$206.4 million, or a purchase cost of 14.0% of face value. The estimated future collections at acquisition for all portfolios purchased during the three months ended September 30, 2016 amounted to \$386.5 million. During the three months ended September 30, 2015, the Company purchased receivable portfolios with a face value of \$2.1 billion for \$187.2 million, or a purchase cost of 9.0% of face value. The estimated future collections at acquisition for all portfolios purchased during the three months ended September 30, 2015 amounted to \$336.4 million.

During the nine months ended September 30, 2016, the Company purchased receivable portfolios with a face value of \$7.9 billion for \$696.2 million, or a purchase cost of 8.9% of face value. The estimated future collections at acquisition for all portfolios purchased during the nine months ended September 30, 2016 amounted to \$1.3 billion.

During the nine months ended September 30, 2015, the Company purchased receivable portfolios with a face value of \$8.7 billion for \$731.1 million, or a purchase cost of 8.4% of face value. Purchases of charged-off credit card portfolios during the nine months ended September 30, 2015, include \$216.0 million of portfolios acquired in connection with the dlc Acquisition. The estimated future collections at acquisition for all portfolios purchased during the nine months ended September 30, 2015 amounted to \$1.3 billion.

All collections realized after the net book value of a portfolio has been fully recovered (“Zero Basis Portfolios”) are recorded as revenue (“Zero Basis Revenue”). During the three months ended September 30, 2016 and 2015, Zero Basis Revenue was approximately \$40.0 million and \$31.8 million, respectively. During the nine months ended September 30, 2016 and 2015, Zero Basis Revenue was approximately \$105.3 million and \$74.3 million, respectively.

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The following tables summarize the changes in the balance of the investment in receivable portfolios during the following periods (in thousands, except percentages):

|   | Three Months Ended September 30, 2016 |               |            |             |
|---|---------------------------------------|---------------|------------|-------------|
|   | Accrual Basis                         | Cost Recovery | Zero Basis | Total       |
|   | Portfolios                            | Portfolios    | Portfolios |             |
| Balance, beginning of period                          | \$2,465,967                           | \$ 3,626      | \$ —       | \$2,469,593 |
| Purchases of receivable portfolios                    | 206,359                               | —             | —          | 206,359     |
| Gross collections <sup>(1)</sup>                      | (366,321 )                            | (706 )        | (39,934 )  | (406,961 )  |
| Put-backs and Recalls <sup>(2)</sup>                  | (3,103 )                              | —             | (57 )      | (3,160 )    |
| Foreign currency adjustments                          | (27,361 )                             | (173 )        | —          | (27,534 )   |
| Revenue recognized                                    | 212,664                               | —             | 38,317     | 250,981     |
| Portfolio (allowance) reversals, net                  | (93,121 )                             | —             | 1,674      | (91,447 )   |
| Balance, end of period                                | \$2,395,084                           | \$ 2,747      | \$ —       | \$2,397,831 |
| Revenue as a percentage of collections <sup>(3)</sup> | 58.1                                  | % 0.0         | % 96.0%    | 61.7 %      |

|   | Three Months Ended September 30, 2015 |               |            |             |
|---|---------------------------------------|---------------|------------|-------------|
|   | Accrual Basis                         | Cost Recovery | Zero Basis | Total       |
|   | Portfolios                            | Portfolios    | Portfolios |             |
| Balance, beginning of period                          | \$2,343,864                           | \$ 7,903      | \$ —       | \$2,351,767 |
| Purchases of receivable portfolios                    | 187,180                               | —             | —          | 187,180     |
| Gross collections <sup>(1)</sup>                      | (388,822 )                            | (1,126 )      | (31,805 )  | (421,753 )  |
| Put-backs and Recalls <sup>(2)</sup>                  | (5,677 )                              | (1 )          | (37 )      | (5,715 )    |
| Foreign currency adjustments                          | (52,505 )                             | (1,273 )      | —          | (53,778 )   |
| Revenue recognized                                    | 240,039                               | —             | 28,745     | 268,784     |
| Portfolio (allowance) reversals, net                  | (6,358 )                              | —             | 3,097      | (3,261 )    |
| Balance, end of period                                | \$2,317,721                           | \$ 5,503      | \$ —       | \$2,323,224 |
| Revenue as a percentage of collections <sup>(3)</sup> | 61.7                                  | % 0.0         | % 90.4%    | 63.7 %      |

(1) Does not include amounts collected on behalf of others.

Put-backs represent accounts that are returned to the seller in accordance with the respective purchase agreement

(2) (“Put-Backs”). Recalls represent accounts that are recalled by the seller in accordance with the respective purchase agreement (“Recalls”).

(3) Revenue as a percentage of collections excludes the effects of net portfolio allowances or net portfolio allowance reversals.

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|   | Nine Months Ended September 30, 2016 |                          |                       | Total        |
|---|--------------------------------------|--------------------------|-----------------------|--------------|
|   | Accrual Basis Portfolios             | Cost Recovery Portfolios | Zero Basis Portfolios |              |
| Balance, beginning of period                          | \$2,436,054                          | \$ 4,615                 | \$ —                  | \$2,440,669  |
| Purchases of receivable portfolios                    | 696,228                              | —                        | —                     | 696,228      |
| Transfer of portfolios                                | (96 )                                | 96                       | —                     | —            |
| Gross collections <sup>(1)</sup>                      | (1,181,546 )                         | (2,063 )                 | (105,257 )            | (1,288,866 ) |
| Put-backs and Recalls <sup>(2)</sup>                  | (19,680 )                            | (11 )                    | (19 )                 | (19,710 )    |
| Foreign currency adjustments                          | (127,680 )                           | 110                      | —                     | (127,570 )   |
| Revenue recognized                                    | 683,752                              | —                        | 100,105               | 783,857      |
| Portfolio (allowance) reversals, net                  | (91,948 )                            | —                        | 5,171                 | (86,777 )    |
| Balance, end of period                                | \$2,395,084                          | \$ 2,747                 | \$ —                  | \$2,397,831  |
| Revenue as a percentage of collections <sup>(3)</sup> | 57.9 %                               | 0.0 %                    | 95.1 %                | 60.8 %       |

|   | Nine Months Ended September 30, 2015 |                          |                       | Total        |
|---|--------------------------------------|--------------------------|-----------------------|--------------|
|   | Accrual Basis Portfolios             | Cost Recovery Portfolios | Zero Basis Portfolios |              |
| Balance, beginning of period                          | \$2,131,084                          | \$ 12,476                | \$ —                  | \$2,143,560  |
| Purchases of receivable portfolios                    | 731,114                              | —                        | —                     | 731,114      |
| Gross collections <sup>(1)</sup>                      | (1,205,717 )                         | (4,351 )                 | (74,080 )             | (1,284,148 ) |
| Put-backs and Recalls <sup>(2)</sup>                  | (9,652 )                             | (20 )                    | (229 )                | (9,901 )     |
| Foreign currency adjustments                          | (54,753 )                            | (2,602 )                 | 20                    | (57,335 )    |
| Revenue recognized                                    | 731,196                              | —                        | 64,780                | 795,976      |
| Portfolio (allowance) reversals, net                  | (5,551 )                             | —                        | 9,509                 | 3,958        |
| Balance, end of period                                | \$2,317,721                          | \$ 5,503                 | \$ —                  | \$2,323,224  |
| Revenue as a percentage of collections <sup>(3)</sup> | 60.6 %                               | 0.0 %                    | 87.4 %                | 62.0 %       |

(1) Does not include amounts collected on behalf of others.

(2) Put-backs represent accounts that are returned to the seller in accordance with the respective purchase agreement.

(2) Recalls represent accounts that are recalled by the seller in accordance with the respective purchase agreement.

(3) Revenue as a percentage of collections excludes the effects of net portfolio allowances or net portfolio allowance reversals.

The following table summarizes the change in the valuation allowance for investment in receivable portfolios during the periods presented (in thousands):

|                                    | Valuation Allowance                   |          |                                      |           |
|------------------------------------|---------------------------------------|----------|--------------------------------------|-----------|
|                                    | Three Months Ended September 30, 2016 |          | Nine Months Ended September 30, 2015 |           |
| Balance at beginning of period     | \$55,918                              | \$68,454 | \$60,588                             | \$75,673  |
| Provision for portfolio allowances | 94,011                                | 8,322    | 94,011                               | 8,322     |
| Reversal of prior allowances       | (2,564 )                              | (5,061 ) | (7,234 )                             | (12,280 ) |
| Balance at end of period           | \$147,365                             | \$71,715 | \$147,365                            | \$71,715  |

#### Note 8: Deferred Court Costs, Net

The Company pursues legal collections using a network of attorneys that specialize in collection matters and through its internal legal channel. The Company generally pursues collections through legal means only when it believes a consumer has sufficient assets to repay their indebtedness but has, to date, been unwilling to pay. In order to pursue legal collections the Company is required to pay certain upfront costs to the applicable courts that are recoverable from the consumer (“Deferred Court Costs”).



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The Company capitalizes Deferred Court Costs in its consolidated financial statements and provides a reserve for those costs that it believes will ultimately be uncollectible. The Company determines the reserve based on an estimated court cost recovery rate established based on its analysis of historical court costs recovery data. Based on recent trends of historical court costs recovery data, the Company noted a decrease in the estimated court cost recovery rate in the United Kingdom. Based on the revised estimated court cost recovery rate, the Company recorded an additional court costs reserve of approximately \$11.3 million during the three months ended September 30, 2016. The Company estimates deferral periods for Deferred Court Costs based on jurisdiction and nature of litigation. The Company writes off any Deferred Court Costs not recovered within the respective deferral period. Collections received from debtors are first applied against related court costs with the balance applied to the debtors' account balance.

Deferred Court Costs for the deferral period consist of the following as of the dates presented (in thousands):

|                       | September 30,<br>2016 | December 31,<br>2015 |
|-----------------------|-----------------------|----------------------|
| Court costs advanced  | \$ 646,399            | \$ 636,922           |
| Court costs recovered | (257,575 )            | (242,899 )           |
| Court costs reserve   | (331,735 )            | (318,784 )           |
| Deferred court costs  | \$ 57,089             | \$ 75,239            |

A roll forward of the Company's court cost reserve is as follows (in thousands):

|   | Court Cost Reserve |             |                   |             |
|---|--------------------|-------------|-------------------|-------------|
|   | Three Months Ended |             | Nine Months Ended |             |
|   | September 30,      |             | September 30,     |             |
|   | 2016               | 2015        | 2016              | 2015        |
| Balance at beginning of period            | \$(319,651)        | \$(298,955) | \$(318,784)       | \$(279,572) |
| Provision for court costs                 | (25,599 )          | (22,434 )   | (55,976 )         | (59,897 )   |
| Net down of reserve after deferral period | 12,955             | 11,924      | 40,028            | 30,284      |
| Effect of foreign currency translation    | 560                | 545         | 2,997             | 265         |
| Balance at end of period                  | \$(331,735)        | \$(308,920) | \$(331,735)       | \$(308,920) |

Note 9: Other Assets

Other assets consist of the following (in thousands):

|                                     | September 30,<br>2016 | December 31,<br>2015 |
|-------------------------------------|-----------------------|----------------------|
| Deferred tax assets                 | \$ 44,087             | \$ 12,695            |
| Identifiable intangible assets, net | 31,113                | 15,712               |
| Prepaid income taxes                | 28,729                | 25,839               |
| Other financial receivables         | 22,047                | 11,275               |
| Prepaid expenses                    | 15,766                | 21,872               |
| Service fee receivables             | 11,045                | 13,708               |
| Receivable from seller              | 5,388                 | 8,605                |
| Security deposits                   | 2,967                 | 2,368                |
| Derivative instruments              | 1,466                 | 718                  |
| Other                               | 43,795                | 35,970               |
| Total                               | \$ 206,403            | \$ 148,762           |

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## Note 10: Debt

The Company is in compliance with all covenants under its financing arrangements. The components of the Company's consolidated debt and capital lease obligations were as follows (in thousands):

|  | September 30, December 31, |              |
|--|----------------------------|--------------|
|  | 2016                       | 2015         |
| Encore revolving credit facility               | \$ 567,000                 | \$ 627,000   |
| Encore term loan facility                      | 134,031                    | 143,078      |
| Encore senior secured notes                    | 14,407                     | 28,750       |
| Encore convertible notes                       | 448,500                    | 448,500      |
| Less: Debt discount                            | (34,502 )                  | (41,867 )    |
| Cabot senior secured notes                     | 1,242,359                  | 1,360,000    |
| Add: Debt premium                              | 39,516                     | 53,440       |
| Less: Debt discount                            | (2,440 )                   | (3,184 )     |
| Cabot senior revolving credit facility         | 114,321                    | 54,089       |
| Preferred equity certificates                  | 211,620                    | 221,516      |
| Capital lease obligations                      | 5,949                      | 11,054       |
| Other  | 140,630                    | 83,342       |
|  | 2,881,391                  | 2,985,718    |
| Less: debt issuance costs, net of amortization | (32,948 )                  | (41,655 )    |
| Total  | \$ 2,848,443               | \$ 2,944,063 |

## Encore Revolving Credit Facility and Term Loan Facility

On March 24, 2016, the Company amended its revolving credit facility and term loan facility pursuant to Amendment No. 3 to the Second Amended and Restated Credit Agreement (as amended, the "Restated Credit Agreement"). The Restated Credit Agreement includes a revolving credit facility of \$742.6 million (the "Revolving Credit Facility"), a term loan facility of \$158.8 million (the "Term Loan Facility," and together with the Revolving Credit Facility, the "Senior Secured Credit Facilities"), and an accordion feature that allows the Company to increase the Senior Secured Credit Facilities by an additional \$250.0 million (\$55.0 million of which was exercised in November 2015). Including the accordion feature, the maximum amount that can be borrowed under the Restated Credit Agreement is \$1.1 billion. The Restated Credit Agreement expires in February 2019, except with respect to two subbranches of the Term Loan Facility of \$60.0 million and \$6.3 million, maturing in February 2017 and November 2017, respectively. Provisions of the Restated Credit Agreement include, but are not limited to:

The Revolving Credit Facility of \$742.6 million that expires in February 2019, with interest at a floating rate equal to, at the Company's option, either: (1) reserve adjusted London Interbank Offered Rate ("LIBOR"), plus a spread that ranges from 250 to 300 basis points depending on the cash flow leverage ratio of Encore and its restricted subsidiaries; or (2) alternate base rate, plus a spread that ranges from 150 to 200 basis points depending on the cash flow leverage ratio of Encore and its restricted subsidiaries. "Alternate base rate," as defined in the Restated Credit Agreement, means the highest of (i) the per annum rate which the administrative agent publicly announces from time to time as its prime lending rate, (ii) the federal funds effective rate from time to time, plus 0.5% per annum, (iii) reserved adjusted LIBOR determined on a daily basis for a one month interest period, plus 1.0% per annum or (iv) zero;

A \$92.5 million term loan maturing on February 25, 2019, with interest at a floating rate equal to, at the Company's option, either: (1) reserve adjusted LIBOR, plus a spread that ranges from 250 to 300 basis points, depending on the cash flow leverage ratio of Encore and its restricted subsidiaries; or (2) alternate base rate, plus a spread that ranges from 150 to 200 basis points, depending on the cash flow leverage ratio of Encore and its restricted subsidiaries. Principal amortizes \$6.9 million in 2016, \$9.3 million in 2017, and \$9.3 million in 2018 with the remaining principal due at the end of the term;

- A \$60.0 million term loan maturing on February 25, 2017, with interest at a floating rate equal to, at the Company's option, either: (1) reserve adjusted LIBOR, plus a spread that ranges from 200 to 250 basis points, depending on the cash flow leverage ratio of Encore and its restricted subsidiaries; or (2) alternate base rate,



plus a spread that ranges

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from 100 to 150 basis points, depending on the cash flow leverage ratio of Encore and its restricted subsidiaries.

Principal amortizes \$4.5 million in 2016 with the remaining principal due at the end of the term;

A \$6.3 million term loan maturing on November 3, 2017, with interest at a floating rate equal to, at the Company's option, either: (1) reserve adjusted LIBOR, plus a spread that ranges from 250 to 300 basis points, depending on the cash flow leverage ratio of Encore and its restricted subsidiaries; or (2) alternate base rate, plus a spread that ranges from 150 to 200 basis points, depending on the cash flow leverage ratio of Encore and its restricted subsidiaries.

Principal amortizes \$0.6 million in 2016 and \$0.5 million in 2017 with the remaining principal due at the end of the term;

A borrowing base under the Revolving Credit Facility equal to (1) the lesser of (i) 30%-35% (depending on the trailing 12-month cost per dollar collected of Encore and its restricted subsidiaries) of all eligible non-bankruptcy estimated remaining collections, currently 33%, plus 55% of eligible estimated remaining collections for consumer receivables subject to bankruptcy, and (ii) the product of the net book value of all receivable portfolios acquired on or after January 1, 2005 multiplied by 95%, minus (2) the sum of the aggregate principal amount outstanding of Encore's Senior Secured Notes (as defined below) plus the aggregate principal amount outstanding under the term loans;

• a maximum cash flow leverage ratio permitted of 2.50:1.00;

• a maximum cash flow secured leverage ratio of 2.00:1.00;

• The allowance of additional unsecured or subordinated indebtedness not to exceed \$1.1 billion;

• Restrictions and covenants, which limit the payment of dividends and the incurrence of additional indebtedness and liens, among other limitations;

• Repurchases of up to \$150.0 million of Encore's common stock after July 9, 2015, subject to compliance with certain covenants and available borrowing capacity;

• A change of control definition that excludes acquisitions of stock by Red Mountain Capital Partners LLC, JCF FPK I, LP and their respective affiliates of up to 50% of the outstanding shares of Encore's voting stock;

• Events of default which, upon occurrence, may permit the lenders to terminate the facility and declare all amounts outstanding to be immediately due and payable;

• A pre-approved acquisition limit of \$225.0 million per fiscal year;

• A basket to allow for investments not to exceed the greater of (1) 200% of the consolidated net worth of Encore and its restricted subsidiaries and (2) an unlimited amount such that after giving effect to the making of any investment, the cash flow leverage ratio is less than 1.25:1.00;

• Collateralization by all assets of the Company, other than the assets of certain foreign subsidiaries and all unrestricted subsidiaries as defined in the Restated Credit Agreement.

At September 30, 2016, the outstanding balance under the Restated Credit Agreement was \$701.0 million, which bore a weighted average interest rate of 3.58% and 3.28% for the three months ended September 30, 2016 and 2015, respectively, and 3.52% and 3.12% for the nine months ended September 30, 2016 and 2015, respectively. Available capacity under the Restated Credit Agreement, subject to borrowing base and applicable debt covenants, was \$175.6 million as of September 30, 2016, not including the \$195.0 million additional capacity provided by the facility's remaining accordion feature.

Encore Senior Secured Notes

In 2010 and 2011 Encore entered into an aggregate of \$75.0 million in senior secured notes with certain affiliates of Prudential Capital Group (the "Senior Secured Notes"). \$25.0 million of the Senior Secured Notes bear an annual interest rate of 7.375%, mature in 2018 and require quarterly principal payments of \$1.25 million. Prior to May 2013, these notes required quarterly payments of interest only. The remaining \$50.0 million of Senior Secured Notes bear an annual interest rate of 7.75%, mature in 2017 and require quarterly principal payments of \$2.5 million. Prior to December 2012 these notes required quarterly interest only payments. As of September 30, 2016, \$6.2 million of the 7.375% Senior Secured Notes and \$8.2 million of the 7.75% Senior Secured Notes, for an aggregate of \$14.4 million, remained outstanding.

The Senior Secured Notes are guaranteed in full by certain of Encore's subsidiaries. The Senior Secured Notes are pari passu with, and are collateralized by the same collateral as, the Senior Secured Credit Facilities. The Senior Secured Notes may be accelerated and become automatically and immediately due and payable upon certain events of default,

including certain events related to insolvency, bankruptcy, or liquidation. Additionally, the Senior Secured Notes may be accelerated at the election of the holder or holders of a majority in principal amount of the Senior Secured Notes upon certain events of default by

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Encore, including the breach of affirmative covenants regarding guarantors, collateral, most favored lender treatment, minimum revolving credit facility commitment or the breach of any negative covenant. If Encore prepays the Senior Secured Notes at any time for any reason, payment will be at the higher of par or the present value of the remaining scheduled payments of principal and interest on the portion being prepaid. The discount rate used to determine the present value is 50 basis points over the then current Treasury Rate corresponding to the remaining average life of the Senior Secured Notes. The covenants are substantially similar to those in the Restated Credit Agreement. Prudential Capital Group and the administrative agent for the lenders of the Restated Credit Agreement have an intercreditor agreement related to their pro rata rights to the collateral, actionable default, powers and duties and remedies, among other topics. The terms of the purchase agreement for the Senior Secured Notes have been amended in connection with amendments to the Restated Credit Agreement in order to align certain provisions between the two agreements.

Encore Convertible Notes

In November and December 2012, Encore sold \$115.0 million aggregate principal amount of 3.0% 2017 Convertible Notes that mature on November 27, 2017 in private placement transactions. In June and July 2013, Encore sold \$172.5 million aggregate principal amount of 3.0% 2020 Convertible Notes that mature on July 1, 2020 in private placement transactions. In March 2014, Encore sold \$161.0 million aggregate principal amount of 2.875% 2021 Convertible Notes that mature on March 15, 2021 in private placement transactions. The interest on these unsecured convertible senior notes (collectively, the “Convertible Notes”), is payable semi-annually.

Prior to the close of business on the business day immediately preceding their respective conversion date (listed below), holders may convert their Convertible Notes under certain circumstances set forth in the applicable Convertible Notes indentures. On or after their respective conversion dates until the close of business on the scheduled trading day immediately preceding their respective maturity date, holders may convert their Convertible Notes at any time. Certain key terms related to the convertible features for each of the Convertible Notes as of September 30, 2016 are listed below.

|   | 2017<br>Convertible<br>Notes | 2020<br>Convertible<br>Notes | 2021<br>Convertible<br>Notes |
|---|------------------------------|------------------------------|------------------------------|
| Initial conversion price                              | \$ 31.56                     | \$ 45.72                     | \$ 59.39                     |
| Closing stock price at date of issuance               | \$ 25.66                     | \$ 33.35                     | \$ 47.51                     |
| Closing stock price date                              | November<br>27, 2012         | June 24,<br>2013             | March 5,<br>2014             |
| Conversion rate (shares per \$1,000 principal amount) | 31.6832                      | 21.8718                      | 16.8386                      |
| Conversion date <sup>(1)</sup>                        | May 27,<br>2017              | January 1,<br>2020           | September<br>15, 2020        |

<sup>(1)</sup> The 2017 Convertible Notes became convertible on January 2, 2014, as certain early conversion events were satisfied. Refer to “Conversion and Earnings Per Share Impact” section below for further details.

In the event of conversion, the 2017 Convertible Notes are convertible into cash up to the aggregate principal amount of the notes. The excess conversion premium may be settled in cash or shares of the Company’s common stock at the discretion of the Company. In the event of conversion, holders of the Company’s 2020 and 2021 Convertible Notes will receive cash, shares of the Company’s common stock or a combination of cash and shares of the Company’s common stock, at the Company’s election. The Company’s current intent is to settle conversions through combination settlement (i.e., convertible into cash up to the aggregate principal amount, and shares of the Company’s common stock or a combination of cash and shares of the Company’s common stock, at the Company’s election, for the remainder). As a result, and in accordance with authoritative guidance related to derivatives and hedging and earnings per share, only the conversion spread is included in the diluted earnings per share calculation, if dilutive. Under such method, the settlement of the conversion spread has a dilutive effect when, during any quarter, the average share price of the Company’s common stock exceeds the initial conversion prices listed in the above table.

Authoritative guidance related to debt with conversion and other options requires that issuers of convertible debt instruments that, upon conversion, may be settled fully or partially in cash, must separately account for the liability

and equity components in a manner that will reflect the entity's nonconvertible debt borrowing rate when interest cost is recognized in subsequent periods. Additionally, debt issuance costs are required to be allocated in proportion to the allocation of the liability and equity components and accounted for as debt issuance costs and equity issuance costs, respectively.

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The debt and equity components, the issuance costs related to the equity component, the stated interest rate, and the effective interest rate for each of the Convertible Notes are listed below (in thousands, except percentages):

|                         | 2017        | 2020        | 2021        |   |
|-------------------------|-------------|-------------|-------------|---|
|                         | Convertible | Convertible | Convertible |   |
|                         | Notes       | Notes       | Notes       |   |
| Debt component          | \$ 100,298  | \$ 140,247  | \$ 143,645  |   |
| Equity component        | \$ 14,702   | \$ 32,253   | \$ 17,355   |   |
| Equity issuance cost    | \$ 788      | \$ 1,106    | \$ 581      |   |
| Stated interest rate    | 3.000       | % 3.000     | % 2.875     | % |
| Effective interest rate | 6.000       | % 6.350     | % 4.700     | % |

The balances of the liability and equity components of all of the Convertible Notes outstanding were as follows (in thousands):

|   | September 30,<br>2016 | December 31,<br>2015 |
|---|-----------------------|----------------------|
| Liability component—principal amount    | \$ 448,500            | \$ 448,500           |
| Unamortized debt discount               | (34,502 )             | (41,867 )            |
| Liability component—net carrying amount | \$ 413,998            | \$ 406,633           |
| Equity component                        | \$ 60,511             | \$ 58,184            |

The debt discount is being amortized into interest expense over the remaining life of the convertible notes using the effective interest rates. Interest expense related to the convertible notes was as follows (in thousands):

|  | Three Months<br>Ended |                       | Nine Months<br>Ended  |                       |
|--|-----------------------|-----------------------|-----------------------|-----------------------|
|  | September 30,<br>2016 | September 30,<br>2015 | September 30,<br>2016 | September 30,<br>2015 |
| Interest expense—stated coupon rate            | \$3,317               | \$3,315               | \$9,925               | \$9,915               |
| Interest expense—amortization of debt discount | 2,501                 | 2,359                 | 7,366                 | 6,947                 |
| Total interest expense—convertible notes       | \$5,818               | \$5,674               | \$17,291              | \$16,862              |

Convertible Notes Hedge Transactions

In order to reduce the risk related to the potential dilution and/or the potential cash payments the Company may be required to make in the event that the market price of the Company's common stock becomes greater than the conversion prices of the Convertible Notes, the Company maintains a hedge program that increases the effective conversion price for each of the Convertible Notes. All of the hedge instruments related to the Convertible Notes have been determined to be indexed to the Company's own stock and meet the criteria for equity classification. In accordance with authoritative guidance, the Company recorded the cost of the hedge instruments as a reduction in additional paid-in capital, and will not recognize subsequent changes in fair value of these financial instruments in its consolidated financial statements.

The details of the hedge program for each of the Convertible Notes are listed below (in thousands, except conversion price):

|                                  | 2017        | 2020        | 2021        |
|----------------------------------|-------------|-------------|-------------|
|                                  | Convertible | Convertible | Convertible |
|                                  | Notes       | Notes       | Notes       |
| Cost of the hedge transaction(s) | \$ 50,595   | \$ 18,113   | \$ 19,545   |
| Initial conversion price         | \$ 31.56    | \$ 45.72    | \$ 59.39    |
| Effective conversion price       | \$ 60.00    | \$ 61.55    | \$ 83.14    |

Conversion and Earnings Per Share Impact

During the quarter ending December 31, 2013, the closing price of the Company's common stock exceeded 130% of the conversion price of the 2017 Convertible Notes for more than 20 trading days during a 30 consecutive trading day period, thereby satisfying one of the early conversion events. As a result, the 2017 Convertible Notes became convertible on demand effective January 2, 2014, and the holders were notified that they could elect to submit their

2017 Convertible Notes for

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conversion. The carrying value of the 2017 Convertible Notes continues to be reported as debt as the Company intends to draw on the Revolving Credit Facility or use cash on hand to settle the principal amount of any such conversions in cash. No gain or loss was recognized when the debt became convertible. The estimated fair value of the 2017 Convertible Notes was approximately \$115.3 million as of September 30, 2016. In addition, upon becoming convertible, a portion of the equity component that was recorded at the time of the issuance of the 2017 Convertible Notes was considered redeemable and that portion of the equity was reclassified to temporary equity in the Company's condensed consolidated statements of financial condition. Such amount was determined based on the cash consideration to be paid upon conversion and the carrying amount of the debt. Upon conversion, the holders of the 2017 Convertible Notes will be paid in cash for the principal amount. The excess conversion premium may be settled in cash or shares of the Company's common stock at the discretion of the Company. As a result, the Company reclassified \$3.8 million of the equity component to temporary equity as of September 30, 2016. If a conversion event takes place, this temporary equity balance will be recalculated based on the difference between the 2017 Convertible Notes principal and the debt carrying value. If the 2017 Convertible Notes are settled, an amount equal to the fair value of the liability component, immediately prior to the settlement, will be deducted from the fair value of the total settlement consideration transferred and allocated to the liability component. Any difference between the amount allocated to the liability and the net carrying amount of the 2017 Convertible Notes (including any unamortized debt issue costs and discount) will be recognized in earnings as a gain or loss on debt extinguishment. Any remaining consideration is allocated to the reacquisition of the equity component and will be recognized as a reduction in stockholders' equity.

None of the 2017 Convertible Notes have been converted since they became convertible.

**Cabot Senior Secured Notes**

On September 20, 2012, Cabot Financial (Luxembourg) S.A. ("Cabot Financial"), an indirect subsidiary of Encore, issued £265.0 million (approximately \$438.4 million) in aggregate principal amount of 10.375% Senior Secured Notes due 2019 (the "Cabot 2019 Notes"). Interest on the Cabot 2019 Notes is payable semi-annually, in arrears, on April 1 and October 1 of each year.

On August 2, 2013, Cabot Financial issued £100.0 million (approximately \$151.7 million) in aggregate principal amount of 8.375% Senior Secured Notes due 2020 (the "Cabot 2020 Notes"). Interest on the Cabot 2020 Notes is payable semi-annually, in arrears, on February 1 and August 1 of each year.

On March 27, 2014, Cabot Financial issued £175.0 million (approximately \$291.8 million) in aggregate principal amount of 6.500% Senior Secured Notes due 2021 (the "Cabot 2021 Notes"). Interest on the Cabot 2021 Notes is payable semi-annually, in arrears, on April 1 and October 1 of each year.

On October 6, 2016, Cabot Financial issued £350.0 million (approximately \$442.6 million) in aggregate principal amount of 7.50% Senior Secured Notes due 2023 (the "Cabot 2023 Notes" and, together with the Cabot 2019 Notes, the Cabot 2020 Notes and the Cabot 2021 Notes, the "Cabot Notes"). Interest on the Cabot 2023 Notes is payable semi-annually, in arrears, on April 1 and October 1 of each year. The proceeds of the Cabot 2023 Notes were used to (1) redeem in full the Cabot 2019 Notes, (2) partially repay amounts outstanding under the Cabot Credit Facility (defined below), (3) pay accrued interest on the Cabot 2019 Notes, and (4) pay fees and expenses in relation to the offering of the Cabot 2023 Notes. Refer to Note 16, "Subsequent Events", for further details of the Cabot 2023 Notes. The Cabot Notes are fully and unconditionally guaranteed on a senior secured basis by the following indirect subsidiaries of the Company: Cabot Credit Management Limited ("CCM"), Cabot Financial Limited, and all material subsidiaries of Cabot Financial Limited (other than Cabot Financial and Marlin Intermediate Holdings plc). The Cabot Notes are secured by a first ranking security interest in all the outstanding shares of Cabot Financial and the guarantors (other than CCM and Marlin Midway Limited) and substantially all the assets of Cabot Financial and the guarantors (other than CCM). Subject to the Intercreditor Agreement described below under "-Cabot Senior Revolving Credit Facility", the guarantees provided in respect of the Cabot Notes are pari passu with each such guarantee given in respect of the Cabot Floating Rate Notes, Marlin Bonds and the Cabot Credit Facility described below.

On November 11, 2015, Cabot Financial (Luxembourg) II S.A. ("Cabot Financial II"), an indirect subsidiary of Encore, issued €310.0 million (approximately \$332.2 million) in aggregate principal amount of Senior Secured Floating Rate Notes due 2021 (the "Cabot Floating Rate Notes"). The Cabot Floating Rate Notes were issued at a 1%, or €3.1 million



(approximately \$3.4 million), original issue discount, which is being amortized over the life of the notes and included as interest expense in the Company's consolidated statements of operations. The Cabot Floating Rate Notes bear interest at a rate equal to three-month EURIBOR plus 5.875% per annum, reset quarterly. Interest on the Cabot Floating Rate Notes is payable quarterly in arrears on February 15, May 15, August 15 and November 15 of each year, beginning on February 15, 2016. The Cabot Floating Rate Notes will mature on November 15, 2021.

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The Cabot Floating Rate Notes are fully and unconditionally guaranteed on a senior secured basis by the following indirect subsidiaries of the Company: CCM, Cabot Financial Limited and all material subsidiaries of Cabot Financial Limited (other than Cabot Financial II and Marlin Intermediate Holdings plc). The Cabot Floating Rate Notes are secured by a first-ranking security interest in all the outstanding shares of Cabot Financial II and the guarantors (other than CCM and Marlin Midway Limited) and substantially all the assets of Cabot Financial II and the guarantors (other than CCM).

On July 25, 2013, Marlin Intermediate Holdings plc (“Marlin”), an indirect subsidiary of Cabot, issued £150.0 million (approximately \$246.5 million) in aggregate principal amount of 10.5% Senior Secured Notes due 2020 (the “Marlin Bonds”). Interest on the Marlin Bonds is payable semi-annually, in arrears, on February 1 and August 1 of each year. Cabot assumed the Marlin Bonds as a result of the acquisition of Marlin. The carrying value of the Marlin Bonds was adjusted to approximately \$284.2 million to reflect the fair value of the Marlin Bonds at the time of acquisition.

The Marlin Bonds are fully and unconditionally guaranteed on a senior secured basis by Cabot Financial Limited and each of Cabot Financial Limited’s material subsidiaries other than Marlin Intermediate Holdings plc, each of which is an indirect subsidiary of the Company. Subject to the Intercreditor Agreement described below under “-Cabot Senior Revolving Credit Facility”, the guarantees provided in respect of the Marlin Bonds are pari passu with each such guarantee given in respect of the Cabot Notes, the Cabot Floating Rate Notes and the Cabot Credit Facility.

Interest expense related to the Cabot Notes, Cabot Floating Rate Notes and Marlin Bonds was as follows (in thousands):

|   | Three Months Ended |          | Nine Months Ended |          |
|---|--------------------|----------|-------------------|----------|
|   | September 30,      |          | September 30,     |          |
|   | 2016               | 2015     | 2016              | 2015     |
| Interest expense—stated coupon rate               | \$25,870           | \$24,394 | \$81,359          | \$72,395 |
| Interest income—accretion of debt premium         | (2,542 )           | (2,771 ) | (7,854 )          | (7,978 ) |
| Interest expense—amortization of debt discount    | 119                | —        | 503               | —        |
| Total interest expense—Cabot senior secured notes | \$23,447           | \$21,623 | \$74,008          | \$64,417 |

At September 30, 2016, the outstanding balance on the Cabot Notes, Cabot Floating Rate Notes and Marlin Bonds was \$1.2 billion.

#### Cabot Senior Revolving Credit Facility

On September 20, 2012, Cabot Financial (UK) Limited (“Cabot Financial UK”) entered into an agreement for a senior committed revolving credit facility of £50.0 million (approximately \$82.7 million) (the “Cabot Credit Agreement”). Since such date there have been a number of amendments made, including, but not limited to, increases in the lenders’ total commitments thereunder. On October 6, 2016, Cabot Financial UK amended and restated its existing senior secured revolving credit facility agreement to, among other things, increase the total committed amount of the facility to £250.0 million (approximately \$316.2 million), extend the termination date to September 24, 2019 and decrease the interest rate from LIBOR (or EURIBOR for any loan drawn in euro) plus 3.5% to LIBOR (or EURIBOR for any loan drawn in euro) plus 3.25% (as amended and restated, the “Cabot Credit Facility”). The Cabot Credit Facility also includes an uncommitted accordion provision which will allow the facility to be increased by an additional £50.0 million, subject to obtaining the requisite commitments and compliance with the terms of Cabot Financial UK’s other indebtedness, among other conditions precedent.

The Cabot Credit Facility expires in September 2019, and includes the following key provisions:

• Interest at LIBOR (or EURIBOR for any loan drawn in euro) plus 3.5% until October 5, 2016 and LIBOR (or EURIBOR for any loan drawn in euro) plus 3.25% thereafter;

• A restrictive covenant that limits the loan to value ratio to 0.75 in the event that the Cabot Credit Facility is more than 20% utilized;

• A restrictive covenant that limits the super senior loan (i.e. the Cabot Credit Facility and any super priority hedging liabilities) to value ratio to 0.25 in the event that the Cabot Credit Facility is more than 20% utilized;

• Additional restrictions and covenants which limit, among other things, the payment of dividends and the incurrence of additional indebtedness and liens; and

- Events of default which, upon occurrence, may permit the lenders to terminate the Cabot Credit Facility and declare all amounts outstanding to be immediately due and payable.

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The Cabot Credit Facility is unconditionally guaranteed by the following indirect subsidiaries of the Company: CCM, Cabot Financial Limited, and all material subsidiaries of Cabot Financial Limited. The Cabot Credit Facility is secured by first ranking security interests in all the outstanding shares of Cabot Financial UK and the guarantors (other than CCM) and substantially all the assets of Cabot Financial UK and the guarantors (other than CCM). Pursuant to the terms of intercreditor agreements entered into with respect to the relative positions of the Cabot Notes, the Cabot Floating Rate Notes, the Marlin Bonds and the Cabot Credit Facility, any liabilities in respect of obligations under the Cabot Credit Facility that are secured by assets that also secure the Cabot Notes, the Cabot Floating Rate Notes and the Marlin Bonds will receive priority with respect to any proceeds received upon any enforcement action over any such assets.

At September 30, 2016, the outstanding borrowings under the Cabot Credit Facility were approximately \$114.3 million. The weighted average interest rate was 3.89% and 3.88% for the three months ended September 30, 2016 and 2015, respectively, and 3.97% and 3.86% for the nine months ended September 30, 2016 and 2015, respectively.

Preferred Equity Certificates

On July 1, 2013, the Company, through its wholly owned subsidiary Encore Europe Holdings, S.a.r.l. (“Encore Europe”), completed the acquisition of Cabot (the “Cabot Acquisition”) by acquiring 50.1% of the equity interest in Janus Holdings S.a.r.l. (“Janus Holdings”). Encore Europe purchased from J.C. Flowers: (i) E Bridge preferred equity certificates issued by Janus Holdings, with a face value of £10,218,574 (approximately \$15.5 million) (and any accrued interest thereof) (the “E Bridge PECs”), (ii) E preferred equity certificates issued by Janus Holdings with a face value of £96,729,661 (approximately \$147.1 million) (and any accrued interest thereof) (the “E PECs”), (iii) 3,498,563 E shares of Janus Holdings (the “E Shares”), and (iv) 100 A shares of Cabot Holdings S.a.r.l. (“Cabot Holdings”), the direct subsidiary of Janus Holdings, for an aggregate purchase price of approximately £115.1 million (approximately \$175.0 million). The E Bridge PECs, E PECs, and E Shares represent 50.1% of all of the issued and outstanding equity and debt securities of Janus Holdings. The remaining 49.9% of Janus Holdings’ equity and debt securities are owned by J.C. Flowers and include: (a) J Bridge PECs with a face value of £10,177,781 (approximately \$15.5 million), (b) J preferred equity certificates with a face value of £96,343,515 (approximately \$146.5 million) (the “J PECs”), (c) 3,484,597 J shares of Janus Holdings (the “J Shares”), and (d) 100 A shares of Cabot Holdings.

All of the PECs accrue interest at 12% per annum. Since PECs are legal form debt, the J Bridge PECs, J PECs and any accrued interests thereof are classified as liabilities and are included in debt in the Company’s accompanying condensed consolidated statements of financial condition. In addition, certain other minority owners hold PECs at the Cabot Holdings level (the “Management PECs”). These PECs are also included in debt in the Company’s accompanying condensed consolidated statements of financial condition. The E Bridge PECs and E PECs held by the Company, and their related interest eliminate in consolidation and therefore are not included in debt in the Company’s condensed consolidated statements of financial condition. The J Bridge PECs, J PECs, and the Management PECs do not require the payment of cash interest expense as they have characteristics similar to equity with a preferred return. The ultimate payment of the accumulated interest would be satisfied only in connection with the disposition of the noncontrolling interests of J.C. Flowers and management.

On June 20, 2014, Encore Europe converted all of its E Bridge PECs into E Shares and E PECs, and J.C. Flowers converted all of its J Bridge PECs into J Shares and J PECs in proportion to the number of E Shares and E PECs, or J Shares and J PECs, as applicable, outstanding on the closing date of the Cabot Acquisition.

As of September 30, 2016, the outstanding balance of the PECs, including accrued interest, was approximately \$211.6 million.

Capital Lease Obligations

The Company has capital lease obligations primarily for computer equipment. As of September 30, 2016, the Company’s combined obligations for capital leases were approximately \$5.9 million. These capital lease obligations require monthly, quarterly or annual payments through 2020 and have implicit interest rates that range from zero to approximately 5.9%.

Note 11: Variable Interest Entity

A VIE is defined as a legal entity whose equity owners do not have sufficient equity at risk, or, as a group, the holders of the equity investment at risk lack any of the following three characteristics: decision-making rights, the obligation

to absorb losses, or the right to receive the expected residual returns of the entity. The primary beneficiary is identified as the variable interest holder that has both the power to direct the activities of the VIE that most significantly affect the entity's economic performance and the obligation to absorb expected losses or the right to receive benefits from the entity that could potentially be significant to the VIE.

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Prior to March 31, 2016, the Company's VIEs included its subsidiary Janus Holdings and its special purpose entity used for the Propel securitization. On March 31, 2016, the Company completed the divestiture of 100% of its membership interests in Propel. Since Propel is the primary beneficiary of the VIE used for securitization, subsequent to the sale of Propel, the Company no longer consolidates this VIE.

Janus Holdings is the indirect parent company of Cabot. The Company has determined that Janus Holdings is a VIE and the Company is the primary beneficiary of the VIE. The key activities that affect Cabot's economic performance include, but are not limited to, operational budgets and purchasing decisions. Through its control of the board of directors of Janus Holdings, the Company controls the key operating activities at Cabot.

Assets recognized as a result of consolidating the VIE do not represent additional assets that could be used to satisfy claims against the Company's general assets. Conversely, liabilities recognized as a result of consolidating the VIE do not represent additional claims on the Company's general assets; rather, they represent claims against the specific assets of the VIE.

The Company evaluates its relationships with its VIE on an ongoing basis to ensure that it continues to be the primary beneficiary.

## Note 12: Income Taxes

Income tax benefits for loss from continuing operations were \$13.8 million and \$6.4 million during the three months ended September 30, 2016 and 2015, respectively. Income tax provisions for income from continuing operations were \$9.8 million and \$23.2 million during the nine months ended September 30, 2016 and 2015, respectively.

The effective tax rates for the respective periods are shown below:

|  | Three Months<br>Ended<br>September 30, |         | Nine Months<br>Ended<br>September 30, |         |
|--|--|---------|---------------------------------------|---------|
|  | 2016                                   | 2015    | 2016                                  | 2015    |
| Federal (benefit) provision                      | (35.0)%                                | (35.0)% | 35.0 %                                | 35.0 %  |
| State (benefit) provision                        | (2.2 )%                                | (2.4 )% | 2.2 %                                 | 2.4 %   |
| International provision (benefit) <sup>(1)</sup> | 16.0 %                                 | (20.5)% | 19.3 %                                | (8.3 )% |
| Permanent items <sup>(2)</sup>                   | 0.3 %                                  | 1.4 %   | 3.3 %                                 | 1.2 %   |
| Tax effect of CFPB / regulatory charges          | 0.0 %                                  | 21.9 %  | 0.0 %                                 | 6.2 %   |
| Other <sup>(3)</sup>                             | (0.1 )%                                | (0.7 )% | (6.7)%                                | 0.2 %   |
| Effective rate                                   | (21.0)%                                | (35.3)% | 53.1 %                                | 36.7 %  |

(1) Relates primarily to lower tax rates on income or loss attributable to international operations.

(2) Represents a provision for nondeductible items.

(3) Includes the effect of discrete items and an IRS audit settlement.

The effective tax rates fluctuated significantly during the periods presented due to the following factors.

In accordance with the authoritative guidance for income taxes, each interim period is considered an integral part of the annual period and tax expense or benefit is measured using an estimated annual effective income tax rate. The estimated annual effective income tax rate for the full year is applied to the respective interim period, taking into account year-to-date amounts and projected amounts for the year. Since the Company operates in foreign countries with varying tax rates that are much lower than the tax rate in the United States, the magnitude of the impact of the results from the international operations have on the Company's quarterly effective tax rate is dependent on the level of income or loss from the international operations in the period. During the third quarter, the Company recorded a large allowance charge on certain portfolio pool groups in Europe and incurred pre-tax losses. As required under the authoritative guidance for interim tax reporting, the Company considered this loss and the related tax benefit in determining its estimated tax rate for the year, which is then applied to the third quarter pre-tax results in determining the quarterly tax expense. Since the loss is tax effected at a much lower tax rate in the United Kingdom, which results in lower tax benefit; and the income in the United States is taxed at a much higher tax rate, which results in higher tax expense, the loss has the effect of increasing the Company's estimated annual tax rate significantly.

The Company's subsidiary in Costa Rica is operating under a 100% tax holiday through December 31, 2018 and a 50% tax holiday for the subsequent four years. The impact of the tax holiday in Costa Rica for the three and nine months ended September 30, 2016 and 2015, was immaterial.

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The Company had gross unrecognized tax benefits, inclusive of penalties and interest, of \$23.9 million and \$58.5 million at September 30, 2016 and December 31, 2015, respectively. These unrecognized tax benefits, if recognized, would result in a net tax benefit of \$10.3 million and \$14.9 million as of September 30, 2016 and December 31, 2015, respectively. The reduction in gross unrecognized tax benefits was due to certain state statute of limitation closing. During the three and nine months ended September 30, 2016, the Company did not provide for U.S. income taxes or foreign withholding taxes on the quarterly undistributed earnings from operations of its subsidiaries operating outside of the United States. Undistributed pre-tax income of these subsidiaries was approximately zero during the three and nine months ended September 30, 2016.

Note 13: Commitments and Contingencies

Litigation and Regulatory

The Company is involved in disputes, legal actions, regulatory investigations, inquiries, and other actions from time to time in the ordinary course of business. The Company, along with others in its industry, is routinely subject to legal actions based on the Fair Debt Collection Practices Act (“FDCPA”), comparable state statutes, the Telephone Consumer Protection Act (“TCPA”), state and federal unfair competition statutes, and common law causes of action. The violations of law investigated or alleged in these actions often include claims that the Company lacks specified licenses to conduct its business, attempts to collect debts on which the statute of limitations has run, has made inaccurate or unsupported assertions of fact in support of its collection actions and/or has acted improperly in connection with its efforts to contact consumers. Such litigation and regulatory actions could involve potential compensatory or punitive damage claims, fines, sanctions, injunctive relief, or changes in business practices. Many continue on for some length of time and involve substantial investigation, litigation, negotiation, and other expense and effort before a result is achieved, and during the process the Company often cannot determine the substance or timing of any eventual outcome.

Except as described in the Company’s Quarterly Report on Form 10-Q for the quarter ended June 30, 2016, at September 30, 2016, there have been no material developments in any of the legal proceedings disclosed in the Company’s Annual Report on Form 10-K for the year ended December 31, 2015.

In certain legal proceedings, the Company may have recourse to insurance or third party contractual indemnities to cover all or portions of its litigation expenses, judgments, or settlements. In accordance with authoritative guidance, the Company records loss contingencies in its financial statements only for matters in which losses are probable and can be reasonably estimated. Where a range of loss can be reasonably estimated with no best estimate in the range, the Company records the minimum estimated liability. The Company continuously assesses the potential liability related to its pending litigation and regulatory matters and revises its estimates when additional information becomes available. In September 2016, the Company recorded \$2.4 million to the TCPA settlement fund in addition to the existing reserve. As of September 30, 2016, other than this additional TCPA reserve, the reserves for the Consumer Finance Protection Bureau (“CFPB”) and ancillary state regulatory matters discussed in the Company’s Annual Report on Form 10-K for the year ended December 31, 2015, the Company has no material reserves for legal matters. Additionally, based on the current status of litigation and regulatory matters, either the estimate of exposure is immaterial to the Company’s financial statements or an estimate cannot yet be determined. The Company’s legal costs are recorded to expense as incurred.

Purchase Commitments

In the normal course of business, the Company enters into forward flow purchase agreements and other purchase commitment agreements. As of September 30, 2016, the Company has entered into agreements to purchase receivable portfolios with a face value of approximately \$2.2 billion for a purchase price of approximately \$346.3 million. Most purchase commitments do not extend past one year.



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## Note 14: Segment Information

The Company conducts business through several operating segments that meet the aggregation criteria under authoritative guidance related to segment reporting. The Company's management relies on internal management reporting processes that provide segment revenue, segment operating income, and segment asset information in order to make financial decisions and allocate resources. Prior to the first quarter 2016 the Company had determined that it had two reportable segments: portfolio purchasing and recovery and tax lien business. As discussed in Note 2, "Discontinued Operations," on March 31, 2016, the Company completed the divestiture of its membership interests in Propel, which comprised the entire tax lien business segment. Propel's operations are presented as discontinued operations in the Company's condensed consolidated statements of operations and comprehensive income. Beginning in the first quarter 2016, the Company has one reportable segment, portfolio purchasing and recovery.

The following table presents information about geographic areas in which the Company operates (in thousands):

|                            | Three Months<br>Ended<br>September 30,<br>2016 |           | Nine Months<br>Ended<br>September 30,<br>2016 |           |
|----------------------------|--|-----------|---|-----------|
| Revenues <sup>(1)</sup> :  |  |           |   |           |
| United States              | \$165,933                                      | \$170,177 | \$502,776                                     | \$535,919 |
| International              |  |           |   |           |
| Europe <sup>(2), (3)</sup> | (9,540   | ) 98,783  | 188,223                                       | 275,521   |
| Other foreign countries    | 23,022   | 9,954     | 66,875  | 27,918    |
|                            | 13,482   | 108,737   | 255,098                                       | 303,439   |
| Total                      | \$179,415                                      | \$278,914 | \$757,874                                     | \$839,358 |

(1) Revenues are attributed to countries based on location of customer.

(2) Based on the financial information that is used to produce the general-purpose financial statements, providing further geographic information is impracticable.

(3) Revenues from Europe during the three and nine months ended September 30, 2016 are net of the allowance charge of \$94.0 million as discussed in Note 7, "Investment in Receivable Portfolios, Net".

## Note 15: Goodwill and Identifiable Intangible Assets

In accordance with authoritative guidance, goodwill is tested for impairment at the reporting unit level annually and in interim periods if indicators of impairment exist or if a decision is made to sell or exit a business. Determining the number of reporting units and the fair value of a reporting unit requires the Company to make judgments and involves the use of significant estimates and assumptions.

In connection with the divestiture of Propel as discussed in Note 2, "Discontinued Operations," the Company wrote-down the entire goodwill balance of \$49.3 million carried at Propel that represented the entire tax lien business reporting unit as of December 31, 2015.

The annual goodwill testing date for the reporting units that are included in the portfolio purchasing and recovery reportable segment is October 1st. There have been no events or circumstances during the nine months ended September 30, 2016 that have required the Company to perform an interim assessment of goodwill carried at these reporting units. Management continues to evaluate and monitor all key factors impacting the carrying value of the Company's recorded goodwill and long-lived assets. Adverse changes in the Company's actual or expected operating results, market capitalization, business climate, economic factors or other negative events that may be outside the control of management could result in a material non-cash impairment charge in the future.

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The Company's goodwill is attributable to reporting units included in its portfolio purchasing and recovery segment as of September 30, 2016 and December 31, 2015. A summary of changes in the carrying amounts of goodwill were as follows (in thousands):

|  | Total     |
|--|-----------|
| Balance, December 31, 2015             | \$924,847 |
| Goodwill acquired                      | 623       |
| Goodwill adjustments <sup>(1)</sup>    | (21,408 ) |
| Effect of foreign currency translation | (84,277 ) |
| Balance, September 30, 2016            | \$819,785 |

Represent adjustments made to preliminary purchase price allocations as a result of obtaining fair value of (1) intangible assets acquired and finalizing certain established deferred income tax associated with prior year business combinations.

The Company's acquired intangible assets are summarized as follows (in thousands):

|                         | As of September 30, 2016 |                          |                     | As of December 31, 2015 |                          |                     |
|-------------------------|--------------------------|--------------------------|---------------------|-------------------------|--------------------------|---------------------|
|                         | Gross Carrying Amount    | Accumulated Amortization | Net Carrying Amount | Gross Carrying Amount   | Accumulated Amortization | Net Carrying Amount |
| Customer relationships  | \$23,523                 | \$ (3,014 )              | \$20,509            | \$5,356                 | \$ (903 )                | \$4,453             |
| Developed technologies  | 8,167                    | (3,855 )                 | 4,312               | 8,141                   | (3,793 )                 | 4,348               |
| Trade name and other    | 10,669                   | (4,377 )                 | 6,292               | 10,324                  | (3,413 )                 | 6,911               |
| Total intangible assets | \$42,359                 | \$ (11,246 )             | \$31,113            | \$23,821                | \$ (8,109 )              | \$15,712            |

## Note 16: Subsequent Events

## Cabot Senior Secured Notes

On October 6, 2016, Cabot Financial issued £350.0 million (approximately \$442.6 million) aggregate principal amount of Cabot 2023 Notes. The Cabot 2023 Notes were issued at a price equal to 100% of their face value. The Cabot 2023 Notes were sold in a private placement to qualified institutional buyers pursuant to Rule 144A under the Securities Act of 1933, as amended (the "Securities Act"), and outside the United States to certain non-U.S. persons pursuant to Regulation S under the Securities Act.

The Cabot 2023 Notes have not been and will not be registered under the Securities Act. The Cabot 2023 Notes are guaranteed on a senior secured basis by CCM, Cabot Financial Limited and all material subsidiaries of Cabot Financial Limited (other than Cabot Financial and Marlin Intermediate Holdings plc). The Cabot 2023 Notes were issued pursuant to an Indenture, dated October 6, 2016, between, among others, Cabot Financial, the guarantors and Citibank, N.A., London Branch, as trustee. The Cabot 2023 Notes are secured by a first-ranking security interest in all the outstanding shares of Cabot Financial and the guarantors (other than CCM and Marlin Midway Limited) and substantially all the assets of Cabot Financial and the guarantors (other than CCM).

The Cabot 2023 Notes bear interest at a fixed rate equal to 7.50% per annum. Interest on the Cabot 2023 Notes is payable semi-annually in arrears on April 1 and October 1 of each year, commencing on April 1, 2017. The Cabot 2023 Notes mature on October 1, 2023.

The proceeds from the offering were used to (1) redeem in full the Cabot 2019 Notes, (2) partially repay amounts outstanding under the Cabot Credit Facility, (3) pay accrued interest on the Cabot 2019 Notes, and (4) pay fees and expenses in relation to the offering of the Cabot 2023 Notes.

## Cabot Senior Revolving Credit Facility

On October 6, 2016, Cabot Financial UK, amended and restated its existing senior secured revolving credit facility agreement to, among other things, increase the total committed amount of the facility to £250 million, extend the termination

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date to September 24, 2019 and decrease the interest rate from LIBOR (or EURIBOR for any loan drawn in euro) plus 3.5% to LIBOR (or EURIBOR for any loan drawn in euro) plus 3.25%.

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## Item 2 – Management’s Discussion and Analysis of Financial Condition and Results of Operations

This Quarterly Report on Form 10-Q contains “forward-looking statements” relating to Encore Capital Group, Inc. (“Encore”) and its subsidiaries (which we may collectively refer to as the “Company,” “we,” “our” or “us”) within the meaning of the securities laws. The words “believe,” “expect,” “anticipate,” “estimate,” “project,” “intend,” “plan,” “will,” “may,” and similar expressions often characterize forward-looking statements. These statements may include, but are not limited to, projections of collections, revenues, income or loss, estimates of capital expenditures, plans for future operations, products or services and financing needs or plans, as well as assumptions relating to these matters. Although we believe that the expectations reflected in these forward-looking statements are reasonable, we caution that these expectations or predictions may not prove to be correct or we may not achieve the financial results, savings, or other benefits anticipated in the forward-looking statements. These forward-looking statements are necessarily estimates reflecting the best judgment of our senior management and involve a number of risks and uncertainties, some of which may be beyond our control or cannot be predicted or quantified, that could cause actual results to differ materially from those suggested by the forward-looking statements. Many factors, including but not limited to those set forth in our Annual Report on Form 10-K under “Part I, Item 1A. Risk Factors,” and those set forth in our subsequent Quarterly Reports on Form 10-Q under “Part II, Item 1A, Risk Factors,” could cause our actual results, performance, achievements, or industry results to be very different from the results, performance, achievements or industry results expressed or implied by these forward-looking statements. Our business, financial condition, or results of operations could also be materially and adversely affected by other factors besides those listed. Forward-looking statements speak only as of the date the statements were made. We do not undertake any obligation to update or revise any forward-looking statements to reflect new information or future events, or for any other reason, even if experience or future events make it clear that any expected results expressed or implied by these forward-looking statements will not be realized. In addition, it is generally our policy not to make any specific projections as to future earnings, and we do not endorse projections regarding future performance that may be made by third parties.

## Our Business and Operating Segments

We are an international specialty finance company providing debt recovery solutions for consumers across a broad range of financial assets. We purchase portfolios of defaulted consumer receivables at deep discounts to face value and manage them by working with individuals as they repay their obligations and work toward financial recovery. Defaulted receivables are consumers’ unpaid financial commitments to credit originators, including banks, credit unions, consumer finance companies, commercial retailers, and telecommunication companies. Defaulted receivables may also include receivables subject to bankruptcy proceedings. Through certain subsidiaries, we are a market leader in portfolio purchasing and recovery in the United States, including Puerto Rico. Our subsidiary, Janus Holdings Luxembourg S.a.r.l. (“Janus Holdings”), through its indirectly held U.K.-based subsidiary Cabot Credit Management Limited and its subsidiaries (collectively, “Cabot”), is a market leader in credit management services in the United Kingdom, historically specializing in portfolios consisting of higher balance, semi-performing accounts (i.e., debt portfolios in which over 50% of the accounts have received a payment in three of the last four months immediately prior to the portfolio purchase). Cabot expanded in the United Kingdom with its consolidating acquisition of Hillesden Securities Ltd and its subsidiaries (“dlc”) in June 2015. Our majority-owned subsidiary, Grove Holdings (“Grove”), is a U.K.-based leading specialty investment firm focused on consumer non-performing loans, including insolvencies (in particular, individual voluntary arrangements, or “IVAs”) in the United Kingdom and bank and non-bank receivables in Spain. Our majority-owned subsidiary, Refinancia S.A. (“Refinancia”), through its subsidiaries, is a market leader in debt collection and management in Colombia and Peru. In October 2015, we completed the acquisition of a controlling stake in Baycorp Holdings Pty Limited (“Baycorp”), one of Australasia’s leading debt resolution specialists. On March 31, 2016, we completed the divestiture of our membership interests in Propel Acquisition LLC (“Propel”). Propel represented our entire tax lien business reportable segment prior to the divestiture. Propel’s operations are presented as discontinued operations in our condensed consolidated statements of operations and comprehensive income. Beginning in the first quarter 2016, we conduct business through one reportable segment, portfolio purchasing and recovery.

Our long-term growth strategy involves continuing to invest in our core portfolio purchasing and recovery business, expanding into new geographies, and leveraging our core competencies to explore expansion into adjacent asset

classes.

Government Regulation

United States

As discussed in more detail under “Part I - Item1 - Business - Government Regulation” in our Annual Report on Form 10-K, our U.S. debt purchasing business and collection activities are subject to federal, state and municipal statutes, rules, regulations and ordinances that establish specific guidelines and procedures that debt purchasers and collectors must follow

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when collecting consumer accounts, including among others, specific guidelines and procedures for communicating with consumers and prohibitions on unfair, deceptive or abusive debt collection practices.

For example, the Consumer Finance Protection Bureau (“CFPB”) may adopt new regulations that may affect our industry and our business. In July 2016, the CFPB released an outline of proposals under consideration for its debt collection rulemaking. The proposals are aimed at ensuring debt collectors, among other things: collect the correct debt; limit excessive or disruptive communications; stop collecting or suing for debt without proper documentation; and provide documentation substantiating debt to a consumer upon demand. The outline of proposals was released by the CFPB in preparation for convening a Small Business Review Panel to gather feedback from small industry players, which is the next step in the rulemaking process. In addition to consulting with small business representatives, the CFPB will continue to seek input from the public, consumer groups, industry, and other stakeholders before continuing the rulemaking process. We believe the rulemaking will provide important clarity around key issues for our industry, help raise industry standards, and create a more level playing field for all companies, large and small. Many of the proposals for consideration released by the CFPB are already part of our current operations, however it is not yet possible to predict the precise impact any final rulemaking will have on our operations and operating results. Additionally, the CFPB has supervisory, examination and enforcement authority over our business and is currently examining the collection practices of participants in the consumer debt buying industry. The CFPB has recently engaged in enforcement activity in sectors adjacent to our industry, impacting credit originators, collection firms, and payment processors, among others. The CFPB’s enforcement activity in these sectors, especially in the absence of clear rules or regulatory expectations, can be disruptive as industry participants attempt to define appropriate business practices. As a result of the current regulatory environment, certain current practices or commercial relationships we maintain may be disrupted or impacted by changes in our or third-parties’ business practices or perceptions of elevated risk.

### International

As discussed in more detail under “Part I - Item 1 - Business - Government Regulation” in our Annual Report on Form 10-K, our international operations are affected by foreign statutes, rules and regulations regarding debt collection and debt purchase activities. These statutes, rules, regulations, ordinances, guidelines and procedures are modified from time to time by the relevant authorities charged with their administration, which could affect the way we conduct our business.

In the United Kingdom, Cabot applied for full authorization of its business with the Financial Conduct Authority (“FCA”) in March 2015 and Cabot Credit Management Group Limited (“CCMG”), a Cabot subsidiary, became authorized and regulated by the FCA in March 2016. CCMG appointed other Cabot subsidiaries as its representatives to carry out debt-collecting and debt administration services on its behalf. CCMG assumes full regulatory responsibility for such entities. In addition to the full authorization of its business with the FCA, CCMG has appointed certain individuals who have significant control or influence over the management of the business, known as “Approved Persons,” and who will jointly and severally be liable for the acts and omissions of CCMG and its business affairs. Approved Persons will be subject to statements of principle and codes of practice established and enforced by the FCA.

The FCA has adopted detailed rules relating to conducting consumer credit activities, in addition to putting in place high-level principles and conditions to which it expects businesses and Approved Persons in the sector to adhere. The FCA has the ability to impose significant fines, ban certain individuals from carrying on trade within the financial services industry, cease certain products from being collected upon and in extreme circumstance remove permissions to trade.

As part of its philosophy of continuous improvement, CCMG regularly reviews policy and practice across all of its business units, to ensure that we can evidence an appropriate and consistent level of compliance to the regulatory requirements. The changes made to policy and practice over the last few years have been designed to reflect the FCA’s outcome based approach, which focuses on the actual customer impact and the key behavioral drivers. Examples of changes made include a call framework refresh that enables increased flexibility for call handlers to tailor conversations to reflect the specific customer circumstances and increased focus on the identification of customer vulnerability.

The FCA also requires that debt repayments agreed with consumers are evidenced as affordable to the consumer, this results in a means-based evaluation of proposed repayments, be that one time settlements or installments over time. We believe this, combined with the changes as described above, have gradually resulted in: a reduction in the number of highly discounted near term one-time settlements; an increase in the number of payment plans, including a shift from legal collections to repayment plans; and an increase in the length of existing payment plans. As a result, we have seen a reduction in the amount of collections in the near term and expect a lengthening of our collections curve. CCMG continues to implement and evaluate operational strategies that are designed to increase collections and mitigate the effects of shifting of collections from the near term to later in our collections curve.

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New legislation, the E.U. General Data Protection Regulation (“GDPR”) will replace the current Data Protection Act in 2018. This will introduce significant changes to the data protection regime including but not limited to: the conditions for obtaining consent to process personal data; transparency and providing information to individuals regarding the processing of their personal data; enhanced rights for individuals; notification obligations for personal data breach; and supervisory authorities including a European Data Protection Board (“EDPB”). We have analyzed the GDPR requirements and are working to ensure that we become compliant.

On June 23, 2016, the United Kingdom held a referendum in which voters approved the United Kingdom’s exit from the European Union (the “E.U.”), commonly referred to as “Brexit”. The referendum was advisory, and the terms of any withdrawal are subject to a negotiation period that could last at least two years after the U.K. government formally initiates a withdrawal process. Nevertheless, the referendum has created significant uncertainty about the future relationship between the United Kingdom and the E.U., including with respect to the laws and regulations that will apply as the United Kingdom determines which E.U. laws to replace or replicate in the event of a withdrawal. Additionally, a withdrawal could, among other outcomes, disrupt the free movement of goods, services and people between the United Kingdom and the E.U., undermine bilateral cooperation in key policy areas and significantly disrupt trade between the United Kingdom and the E.U. Given the lack of comparable precedent, it is unclear what financial, trade and legal implications the withdrawal of the United Kingdom from the E.U. will have and how such withdrawal will affect us. The GDPR requirements discussed above will not be impacted by the United Kingdom leaving the E.U.

As a result of the Brexit referendum foreign currency exchange rates have been impacted. In particular, the value of the British Pound has declined as compared to the U.S. dollar and other currencies. This volatility in foreign currencies is expected to continue as the United Kingdom negotiates and executes its exit from the E.U. but it is uncertain over what time period this will occur. A significantly weaker British Pound compared to the U.S. dollar could have a significant negative effect on the Company’s business, financial condition and results of operations.

### Portfolio Purchasing and Recovery

#### United States

We purchase receivables based on robust, account-level valuation methods and employ proprietary statistical and behavioral models across our U.S. operations. These methods and models allow us to value portfolios accurately (and limit the risk of overpaying), avoid buying portfolios that are incompatible with our methods or goals and align the accounts we purchase with our business channels to maximize future collections. As a result, we have been able to realize significant returns from the receivables we acquire. We maintain strong relationships with many of the largest financial service providers in the United States.

While seasonality does not have a material impact on our portfolio purchasing and recovery business, collections are generally strongest in our first calendar quarter, slower in the second and third calendar quarters, and slowest in the fourth calendar quarter. Relatively higher collections in the first quarter could result in a lower cost-to-collect ratio compared to the other quarters, as our fixed costs are relatively constant and applied against a larger collection base. The seasonal impact on our business may also be influenced by our purchasing levels, the types of portfolios we purchase, and our operating strategies.

Collection seasonality can also affect revenue as a percentage of collections, also referred to as our revenue recognition rate. Generally, revenue for each pool group declines steadily over time, whereas collections can fluctuate from quarter to quarter based on seasonality, as described above. In quarters with lower collections (e.g., the fourth calendar quarter), the revenue recognition rate can be higher than in quarters with higher collections (e.g., the first calendar quarter).

In addition, seasonality could have an impact on the relative level of quarterly earnings. In quarters with stronger collections, total costs are higher as a result of the additional efforts required to generate those collections. Since revenue for each pool group declines steadily over time, in quarters with higher collections and higher costs (e.g., the first calendar quarter), all else being equal, earnings could be lower than in quarters with lower collections and lower costs (e.g., the fourth calendar quarter). Additionally, in quarters where a greater percentage of collections come from our legal and agency outsourcing channels, cost to collect will be higher than if there were more collections from our internal collection sites.



Europe

Cabot: Through Cabot, we purchase paying and non-paying receivable portfolios using a proprietary pricing model that utilizes account-level statistical and behavioral data. This model allows Cabot to value portfolios with a high degree of accuracy and quantify portfolio performance in order to maximize future collections. As a result, Cabot has been able to realize significant returns from the assets it has acquired. Cabot maintains strong relationships with many of the largest financial

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services providers in the United Kingdom and continues to expand in the United Kingdom and the rest of Europe with its acquisitions of portfolios and other credit management services providers.

While seasonality does not have a material impact on Cabot's operations, collections are generally strongest in the second and third calendar quarters and slower in the first and fourth quarters, largely driven by the impact of the December holiday season and the New Year holiday, and the related impact on its customers' ability to repay their balances. This drives a higher level of plan defaults over this period, which are typically repaired across the first quarter of the following year. The August vacation season in the United Kingdom also has an unfavorable effect on the level of collections, but this is traditionally compensated for by higher collections in July and September.

Grove: On April 1, 2014, we completed the acquisition of a controlling equity ownership interest in Grove. Grove, through its subsidiaries and affiliates, is a leading specialty investment firm focused on consumer non-performing loans, including insolvencies (in particular, IVAs) in the United Kingdom and bank and non-bank receivables in Spain. Grove purchases portfolio receivables using a proprietary pricing model. This model allows Grove to value portfolios and quantify portfolio performance in order to maximize future collections.

### Latin America

In December 2013, we acquired a majority ownership interest in Refinancia, a market leader in debt collection and management in Colombia and Peru. In addition to purchasing defaulted receivables, Refinancia offers portfolio management services to banks for non-performing loans. Refinancia also specializes in non-traditional niches in the geographic areas in which it operates, including providing financial solutions to individuals who have previously defaulted on their credit obligations. In addition to operations in Colombia and Peru, we evaluate and purchase non-performing loans in other countries in Latin America, including Mexico and Brazil. We also invest in non-performing secured residential mortgages in Latin America.

### Asia Pacific

Through our acquisition of a majority ownership interest in Baycorp in October 2015 (the "Baycorp Acquisition"), we are one of Australia's leading debt resolution specialists. Baycorp specializes in the management of non-performing loans in Australia and New Zealand. In addition to purchasing defaulted receivables, Baycorp offers portfolio management services to banks for non-performing loans.

### Purchases and Collections

#### Portfolio Pricing, Supply and Demand

##### United States

Prices for portfolios offered for sale directly from credit issuers are beginning to decrease after several years of elevated pricing, especially for fresh portfolios. Fresh portfolios are portfolios that are generally transacted within six months of the consumer's account being charged-off by the financial institution. Industry delinquency and charge off rates have been at historic lows, and they are beginning to increase which creates higher volumes of charged-off accounts. We believe the softening in pricing, especially fresh, is primarily due to this anticipated growth in supply. We believe that smaller competitors continue to face difficulties in the portfolio purchasing market because of the high cost to operate due to regulatory pressure and because issuers are being more selective with buyers in the marketplace, resulting in consolidation within the portfolio purchasing and recovery industry. We believe this favors larger participants in this market, such as Encore, because the larger market participants are better able to adapt to these pressures. Furthermore, as smaller competitors limit their participation in or exit the market, it may provide additional opportunities for Encore to purchase portfolios from competitors or to acquire competitors directly.

##### Europe

The U.K. market for charged-off portfolios has grown significantly in recent years driven by a consolidation of sellers and a material backlog of portfolio coming to market from credit issuers who are selling an increasing proportion of their non-performing loans. Prices for portfolios offered for sale directly from credit issuers remain at levels higher than historical averages. We expect that as a result of an increase in available funding to industry participants, and lower return requirements for certain debt purchasers, pricing will remain elevated.

The U.K. insolvency market saw historically low sales volumes from banks in the last twelve months. We expect there will be increased purchasing opportunities once large retail banks start to sell their insolvency portfolios.



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The Spanish consumer and small and medium enterprise non-performing loan market remains significant, with most of the major banks selling portfolios. While competition remains strong in large banking trades, recently there have been multiple complex sales from consolidated regional banks trading at more favorable returns as portfolio sale sizes and an increased asset mix of SME (small and medium enterprise) and other corporate debtors reduce competition. Although pricing has been elevated, we believe that as our U.K. businesses increase in scale and expand to other European markets, and with anticipated improvements in liquidation and improved efficiencies in collections, our margins will remain competitive. Additionally, Cabot's continuing investment in its liquidation channel through litigation has enabled them to collect from consumers who have the ability to pay, but have so far been unwilling to do so.

## Purchases by Type and Geographic Location

The following table summarizes the types and geographic locations of consumer receivable portfolios we purchased during the periods presented (in thousands):

|                                 | Three Months  |           | Nine Months   |           |
|---------------------------------|---------------|-----------|---------------|-----------|
|                                 | Ended         |           | Ended         |           |
|                                 | September 30, |           | September 30, |           |
|                                 | 2016          | 2015      | 2016          | 2015      |
| United States:                  |               |           |               |           |
| Credit card                     | \$131,671     | \$120,883 | \$379,300     | \$347,524 |
| Consumer bankruptcy receivables | 9,914         | 10,978    | 33,776        | 10,978    |
| Subtotal                        | 141,585       | 131,861   | \$413,076     | \$358,502 |
| Europe:                         |               |           |               |           |
| Credit card                     | 30,727        | 37,342    | 207,682       | 338,218   |
| IVA                             | 107           | 4,681     | 2,546         | 7,418     |
| Other                           | 12,133        | —         | 12,133        | 8,460     |
| Subtotal                        | 42,967        | 42,023    | 222,361       | 354,096   |
| Other geographies:              |               |           |               |           |
| Credit card and other           | 21,807        | 13,296    | 60,791        | 18,516    |
| Total purchases                 | \$206,359     | \$187,180 | \$696,228     | \$731,114 |

During the three months ended September 30, 2016, we invested \$206.4 million to acquire consumer receivable portfolios, with face values aggregating \$1.5 billion, for an average purchase price of 14.0% of face value. This is a \$19.2 million, or 10.3%, increase in the amount invested, compared with the \$187.2 million invested during the three months ended September 30, 2015, to acquire consumer receivable portfolios with face values aggregating \$2.1 billion, for an average purchase price of 9.0% of face value.

During the nine months ended September 30, 2016, we invested \$696.2 million to acquire consumer receivable portfolios, with face values aggregating \$7.9 billion, for an average purchase price of 8.9% of face value. This is a \$34.9 million, or 4.8%, decrease in the amount invested, compared with the \$731.1 million invested during the nine months ended September 30, 2015, to acquire consumer receivable portfolios with face values aggregating \$8.7 billion, for an average purchase price of 8.4% of face value.

The increase in capital deployment for the three months ended September 30, 2016, as compared to the corresponding period in the prior year, was primarily the result of increased purchasing volume in the United States due to the improved pricing environment. The decrease in capital deployment for the nine months ended September 30, 2016, as compared to the corresponding period in the prior year, was due to the \$216.0 million of receivable portfolios acquired in connection with the dlc Acquisition in June 2015. Excluding the portfolios acquired in connection with the dlc Acquisition, capital deployment increased during the nine months ended September 30, 2016 as compared to the comparable period in 2015, primarily as a result of increased purchasing volume in the United States and Cabot's investment in Spain, France and Portugal as part of its European expansion strategy.

The average purchase price, as a percentage of face value, varies from period to period depending on, among other factors, the quality of the accounts purchased and the length of time from charge-off to the time we purchase the portfolios. Additionally, the improved pricing environment has not materialized to blend down the average purchase

price as a percentage of face value in the United States.

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## Collections by Channel and Geographic Location

We currently utilize three channels for the collection of our receivables: collection sites, legal collections, and collection agencies. The collection sites channel consists of collections that result from our call centers, direct mail program and online collections. The legal collections channel consists of collections that result from our internal legal channel or from our network of retained law firms. The collection agencies channel consists of collections from third-party collection agencies that we utilize when we believe they can liquidate better or less expensively than we can or to supplement capacity in our internal call centers. The following table summarizes the total collections by collection channel and geographic area (in thousands):

|                                    | Three Months Ended September 30, |            | Nine Months Ended September 30, |              |
|------------------------------------|----------------------------------|------------|---------------------------------|--------------|
|                                    | 2016                             | 2015       | 2016                            | 2015         |
| United States:                     |                                  |            |                                 |              |
| Collection sites                   | \$ 111,753                       | \$ 113,663 | \$ 362,010                      | \$ 374,745   |
| Legal collections                  | 130,985                          | 154,190    | 427,972                         | 480,896      |
| Collection agencies <sup>(1)</sup> | 12,875                           | 16,649     | 41,630                          | 52,702       |
| Subtotal                           | 255,613                          | 284,502    | 831,612                         | 908,343      |
| Europe:                            |                                  |            |                                 |              |
| Collection sites                   | 61,306                           | 65,512     | 180,742                         | 176,169      |
| Legal collections                  | 31,502                           | 24,680     | 94,596                          | 63,616       |
| Collection agencies                | 28,730                           | 38,564     | 100,684                         | 112,136      |
| Subtotal                           | 121,538                          | 128,756    | 376,022                         | 351,921      |
| Other geographies:                 |                                  |            |                                 |              |
| Collection sites                   | 22,518                           | 7,681      | 60,726                          | 22,706       |
| Legal collections                  | 2,634                            | —          | 7,775                           | —            |
| Collection agencies                | 4,658                            | 814        | 12,731                          | 1,178        |
| Subtotal                           | 29,810                           | 8,495      | 81,232                          | 23,884       |
| Total collections                  | \$ 406,961                       | \$ 421,753 | \$ 1,288,866                    | \$ 1,284,148 |

Collections through our collection agency channel in the United States include accounts subject to bankruptcy filings collected by others. Additionally, collection agency collections often include accounts purchased from a competitor where we maintain the collection agency servicing until the accounts can be recalled and placed in our collection channels.

Gross collections decreased by \$14.8 million, or 3.5%, to \$407.0 million during the three months ended September 30, 2016, from \$421.8 million during the three months ended September 30, 2015. The decrease was primarily due to decreased collections in the United States and Europe, partially offset by increased collections in other geographies. The decrease in collections in the United States was primarily due to a decrease in legal collections resulting from temporary delays in receiving media from issuers required to initiate the legal process for a number of accounts. We believe these temporary delays will decrease in the fourth quarter of 2016 and expect increased placements in our legal channel thereafter. In Europe, the decrease in collections was due to the unfavorable impact of foreign currency translation, primarily driven by the weakening of the British Pound against the U.S. dollar. As we continue to expand and enhance our in-house servicing capabilities in Europe, we expect collections to shift from collection agencies to collection sites and legal collections. The increase in legal collections was primarily due to an increase in the accounts placed in the legal channel as we continuously improve our ability to identify consumers that are able, but unwilling, to pay their obligations. In other geographies collections continue to increase as the Company expands internationally. Gross collections increased slightly by \$4.8 million, or 0.4%, to \$1,288.9 million during the nine months ended September 30, 2016, from \$1,284.1 million during the nine months ended September 30, 2015, primarily due to increased collections in Europe and other geographies, offset by a decrease of collections in the United States. The increase in collections in Europe was primarily the result of increased legal collections offset by a decrease in

collection agency collections. The increase in legal collections was primarily due to an increase in the accounts placed in the legal channel as we continuously improve our ability to identify consumers that are able, but unwilling, to pay their obligations. As we continue to expand and enhance our in-house servicing capabilities in Europe, we expect collections to shift from collection agencies to collection sites and legal collections. The increase in collections in Europe was partially offset by the unfavorable impact of foreign currency translation, primarily driven by the weakening of the British Pound against the U.S. dollar. In other geographies collections continue to increase as the Company expands internationally. The decrease of collections in the United States was primarily

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due to a decrease in legal collections resulting from temporary delays in receiving media from issuers required to initiate the legal process for a number of accounts.

## Results of Operations

Results of operations, in dollars and as a percentage of total revenues, were as follows (in thousands, except percentages):

|  | Three Months Ended September 30, |          |             |          |
|--|----------------------------------|----------|-------------|----------|
|  | 2016                             |          | 2015        |          |
| Revenues   |                                  |          |             |          |
| Revenue from receivable portfolios, net                          | \$ 159,534                       | 88.9 %   | \$ 265,523  | 95.2 %   |
| Other revenues   | 19,881                           | 11.1 %   | 13,391      | 4.8 %    |
| Total revenues   | 179,415                          | 100.0 %  | 278,914     | 100.0 %  |
| Operating expenses   |                                  |          |             |          |
| Salaries and employee benefits                                   | 67,783                           | 37.8 %   | 62,995      | 22.6 %   |
| Cost of legal collections  | 56,932                           | 31.7 %   | 58,760      | 21.1 %   |
| Other operating expenses   | 24,131                           | 13.5 %   | 22,217      | 8.0 %    |
| Collection agency commissions                                    | 8,848                            | 4.9 %    | 9,381       | 3.3 %    |
| General and administrative expenses                              | 34,871                           | 19.4 %   | 86,789      | 31.1 %   |
| Depreciation and amortization                                    | 8,032                            | 4.5 %    | 8,043       | 2.9 %    |
| Total operating expenses   | 200,597                          | 111.8 %  | 248,185     | 89.0 %   |
| (Loss) income from operations                                    | (21,182 )                        | (11.8 )% | 30,729      | 11.0 %   |
| Other (expense) income   |                                  |          |             |          |
| Interest expense   | (48,632 )                        | (27.1 )% | (47,816 )   | (17.1 )% |
| Other income (expense)   | 4,100                            | 2.3 %    | (924 )      | (0.4 )%  |
| Total other expense  | (44,532 )                        | (24.8 )% | (48,740 )   | (17.5 )% |
| Loss before income taxes   | (65,714 )                        | (36.6 )% | (18,011 )   | (6.5 )%  |
| Benefit for income taxes   | 13,768                           | 7.6 %    | 6,361       | 2.3 %    |
| Loss from continuing operations                                  | (51,946 )                        | (29.0 )% | (11,650 )   | (4.2 )%  |
| Income from discontinued operations, net of tax                  | —                                | 0.0 %    | 2,286       | 0.8 %    |
| Net loss   | (51,946 )                        | (29.0 )% | (9,364 )    | (3.4 )%  |
| Net loss (income) attributable to noncontrolling interest        | 50,422                           | 28.2 %   | (1,595 )    | (0.5 )%  |
| Net loss attributable to Encore Capital Group, Inc. stockholders | \$(1,524 )                       | (0.8 )%  | \$(10,959 ) | (3.9 )%  |



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|  | Nine Months Ended September 30, |          |  |            |          |  |
|--|---------------------------------|----------|--|------------|----------|--|
|  | 2016                            |          |  | 2015       |          |  |
| Revenues   |                                 |          |  |            |          |  |
| Revenue from receivable portfolios, net                            | \$697,080                       | 92.0 %   |  | \$799,934  | 95.3 %   |  |
| Other revenues   | 60,794                          | 8.0 %    |  | 39,424     | 4.7 %    |  |
| Total revenues   | 757,874                         | 100.0 %  |  | 839,358    | 100.0 %  |  |
| Operating expenses   |                                 |          |  |            |          |  |
| Salaries and employee benefits                                     | 212,924                         | 28.1 %   |  | 194,116    | 23.1 %   |  |
| Cost of legal collections  | 158,047                         | 20.9 %   |  | 170,834    | 20.4 %   |  |
| Other operating expenses   | 75,420                          | 10.0 %   |  | 68,278     | 8.1 %    |  |
| Collection agency commissions                                      | 28,242                          | 3.7 %    |  | 28,532     | 3.4 %    |  |
| General and administrative expenses                                | 103,044                         | 13.6 %   |  | 155,624    | 18.5 %   |  |
| Depreciation and amortization                                      | 26,128                          | 3.4 %    |  | 24,058     | 2.9 %    |  |
| Total operating expenses   | 603,805                         | 79.7 %   |  | 641,442    | 76.4 %   |  |
| Income from operations   | 154,069                         | 20.3 %   |  | 197,916    | 23.6 %   |  |
| Other (expense) income   |                                 |          |  |            |          |  |
| Interest expense   | (149,920 )                      | (19.8 )% |  | (136,369 ) | (16.2 )% |  |
| Other income   | 14,358                          | 1.9 %    |  | 1,588      | 0.1 %    |  |
| Total other expense  | (135,562 )                      | (17.9 )% |  | (134,781 ) | (16.1 )% |  |
| Income before income taxes   | 18,507                          | 2.4 %    |  | 63,135     | 7.5 %    |  |
| Provision for income taxes   | (9,831 )                        | (1.3 )%  |  | (23,174 )  | (2.7 )%  |  |
| Income from continuing operations                                  | 8,676                           | 1.1 %    |  | 39,961     | 4.8 %    |  |
| (Loss) income from discontinued operations, net of tax             | (3,182 )                        | (0.4 )%  |  | 5,827      | 0.7 %    |  |
| Net income   | 5,494                           | 0.7 %    |  | 45,788     | 5.5 %    |  |
| Net loss attributable to noncontrolling interest                   | 48,264                          | 6.4 %    |  | 335        | 0.0 %    |  |
| Net income attributable to Encore Capital Group, Inc. stockholders | \$53,758                        | 7.1 %    |  | \$46,123   | 5.5 %    |  |

## Results of Operations—Cabot

The following table summarizes the operating results contributed by Cabot during the periods presented (in thousands):

|   | Three Months Ended September 30, 2016 |                              |              | Three Months Ended September 30, 2015 |                              |              |
|---|---------------------------------------|------------------------------|--------------|---------------------------------------|------------------------------|--------------|
|   | Janus Holdings                        | Encore Europe <sup>(1)</sup> | Consolidated | Janus Holdings                        | Encore Europe <sup>(1)</sup> | Consolidated |
| Total revenues <sup>(2)</sup>   | \$(12,842)                            | \$—                          | \$(12,842 )  | \$92,641                              | \$—                          | \$ 92,641    |
| Total operating expenses  | (58,074 )                             | —                            | (58,074 )    | (47,203 )                             | —                            | (47,203 )    |
| (Loss) income from operations   | (70,916 )                             | —                            | (70,916 )    | 45,438                                | —                            | 45,438       |
| Interest expense-non-PEC  | (26,472 )                             | —                            | (26,472 )    | (27,564 )                             | —                            | (27,564 )    |
| PEC interest (expense) income   | (11,575 )                             | 5,672                        | (5,903 )     | (12,264 )                             | 6,010                        | (6,254 )     |
| Other income (expense)  | 4,845                                 | —                            | 4,845        | (570 )                                | —                            | (570 )       |
| (Loss) income before income taxes   | (104,118 )                            | 5,672                        | (98,446 )    | 5,040                                 | 6,010                        | 11,050       |
| Benefit (provision) for income taxes                                      | 17,382                                | —                            | 17,382       | (2,037 )                              | —                            | (2,037 )     |
| Net (loss) income   | (86,736 )                             | 5,672                        | (81,064 )    | 3,003                                 | 6,010                        | 9,013        |
| Net loss (income) attributable to noncontrolling interest                 | 12,087                                | 37,250                       | 49,337       | (421 )                                | (1,289 )                     | (1,710 )     |
| Net (loss) income attributable to Encore Capital Group, Inc. stockholders | \$(74,649)                            | \$42,922                     | \$(31,727 )  | \$2,582                               | \$4,721                      | \$ 7,303     |

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|   | Nine Months Ended September 30, 2016 |                              |              | Nine Months Ended September 30, 2015 |                              |              |
|---|--------------------------------------|------------------------------|--------------|--------------------------------------|------------------------------|--------------|
|   | Janus Holdings                       | Encore Europe <sup>(1)</sup> | Consolidated | Janus Holdings                       | Encore Europe <sup>(1)</sup> | Consolidated |
| Total revenues <sup>(2)</sup>   | \$ 168,819                           | \$ —                         | \$ 168,819   | \$ 257,031                           | \$ —                         | \$ 257,031   |
| Total operating expenses  | (159,054 )                           | —                            | (159,054 )   | (136,405 )                           | —                            | (136,405 )   |
| Income from operations  | 9,765                                | —                            | 9,765        | 120,626                              | —                            | 120,626      |
| Interest expense-non-PEC  | (83,323 )                            | —                            | (83,323 )    | (77,297 )                            | —                            | (77,297 )    |
| PEC interest (expense) income   | (36,638 )                            | 17,954                       | (18,684 )    | (36,004 )                            | 17,644                       | (18,360 )    |
| Other income  | 16,243                               | —                            | 16,243       | 485                                  | —                            | 485          |
| (Loss) income before income taxes   | (93,953 )                            | 17,954                       | (75,999 )    | 7,810                                | 17,644                       | 25,454       |
| Benefit (provision) for income taxes                                      | 13,565                               | —                            | 13,565       | (5,561 )                             | —                            | (5,561 )     |
| Net (loss) income   | (80,388 )                            | 17,954                       | (62,434 )    | 2,249                                | 17,644                       | 19,893       |
| Net loss (income) attributable to noncontrolling interest                 | 11,246                               | 34,502                       | 45,748       | (315 )                               | (965 )                       | (1,280 )     |
| Net (loss) income attributable to Encore Capital Group, Inc. stockholders | \$(69,142 )                          | \$ 52,456                    | \$(16,686 )  | \$ 1,934                             | \$ 16,679                    | \$ 18,613    |

(1) Includes only the results of operations related to Janus Holdings and therefore does not represent the complete financial performance of Encore Europe.

(2) Total revenues are net of the portfolio allowance charges recorded on certain pool groups at Cabot during the three months ended September 30, 2016.

For all periods presented, Janus Holdings recognized all interest expense related to the outstanding preferred equity certificates (“PECs”) owed to Encore and other minority shareholders, while the interest income from PECs owed to Encore was recognized at Janus Holdings’ parent company, Encore Europe Holdings, S.a.r.l. (“Encore Europe”), which is a wholly-owned subsidiary of Encore.

#### Comparison of Results of Operations

##### Revenues

Our revenues consist of portfolio revenue and other revenue.

Portfolio revenue consists of accretion revenue and Zero Basis Revenue. Accretion revenue represents revenue derived from pools (quarterly groupings of purchased receivable portfolios) with a cost basis that has not been fully amortized. Revenue from pools with a remaining unamortized cost basis is accrued based on each pool’s effective interest rate applied to each pool’s remaining unamortized cost basis. The cost basis of each pool is increased by revenue earned and decreased by gross collections and portfolio allowances. The effective interest rate is the IRR derived from the timing and amounts of actual cash received and anticipated future cash flow projections for each pool. All collections realized after the net book value of a portfolio has been fully recovered, or Zero Basis Portfolios (“ZBA”), are recorded as revenue, or Zero Basis Revenue. We account for our investment in receivable portfolios utilizing the interest method in accordance with the authoritative guidance for loans and debt securities acquired with deteriorated credit quality. We may incur allowance charges when actual cash flows from our receivable portfolios underperform compared to our expectations or when there is a change in timing of cash flows. Factors that may contribute to underperformance and to the recording of valuation allowances may include both internal as well as external factors. Internal factors that may have an impact on our collections include operational activities, such as the productivity of our collection staff. External factors that may have an impact on our collections include new laws or regulations, new interpretations of existing laws or regulations, and the overall condition of the economy. We record allowance reversals on pool groups that have historic allowance reserves when actual cash flows from these receivable portfolios outperform our expectations. Allowance reversals are included in portfolio revenue.

Other revenues consist primarily of contingent fee income earned on accounts collected on behalf of others, primarily credit originators.

Our operating results are impacted by foreign currency translation, which represents the effect of translating operating results where the functional currency is different than our U.S. dollar reporting currency. The strengthening of the U.S. dollar relative to other foreign currencies has an unfavorable impact on our international revenues, and the weakening of the U.S. dollar relative to other foreign currencies has a favorable impact on our international revenues. Our revenues were impacted by

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foreign currency translation, primarily by the weakening of the British Pound, which devalued against the U.S. dollar by 15.2% and 9.1%, for the three and nine months ended September 30, 2016, respectively, compared to the comparable periods in 2015.

Portfolio revenue was \$159.5 million during the three months ended September 30, 2016, a decrease of \$106.0 million, or 39.9%, compared to \$265.5 million during the three months ended September 30, 2015. Portfolio revenue was \$697.1 million during the nine months ended September 30, 2016, a decrease of \$102.8 million, or 12.9%, compared to revenue of \$799.9 million during the nine months ended September 30, 2015. The decreases in portfolio revenue during the three and nine months ended September 30, 2016 compared to the comparable periods in 2015 were the result of allowance charges recorded on certain pools in Europe and the negative impact of foreign currency translation, primarily from the weakening of the British Pound against the U.S. dollar.

During the three months ended September 30, 2016, we recorded allowance charges of approximately \$94.0 million resulting from delays or shortfalls in near term collections against our forecasts for certain pools in Europe. These allowance charges, net of portfolio allowance reversals on other pools, attributed to the net portfolio allowance of \$91.4 million and \$86.8 million during the three and nine months ended September 30, 2016, respectively. During the three and nine months ended September 30, 2015, we recorded a net portfolio allowance of \$3.3 million and a net portfolio allowance reversal of \$4.0 million, respectively. The net portfolio allowance reversals recorded in 2015 were primarily due to the reversal of remaining allowance reserves for certain ZBA pool groups with cash collections, offset by an \$8.3 million portfolio allowance charge resulting from our settlement with the CFPB.

Additionally, during the quarter ended September 30, 2016, we revised the forecasting methodology we use to value and calculate IRRs on certain portfolios in Europe by extending the collection forecast from 120 months to 180 months. This change was made as a result of (1) our observation that older portfolios in Europe have consistently experienced cash collections beyond 120 months, (2) an expectation that regulatory changes in the United Kingdom resulting in a reduction in the number of highly discounted near term one-time settlements, an increase in the number of payment plans, and an increase in the length of existing payment plans will cause a lengthening of our collections curve, (3) an expectation that, as a result of a higher percentage of semi-performing account purchases in the United Kingdom in recent years, newer vintages will have a larger percentage of collections after 120 months and (4) our increased confidence in our ability to forecast future cash collections to 180 months. The increase in the collection forecast from 120 months to 180 months was applied effective July 1, 2016, to certain portfolios in Europe for which we could accurately forecast through such term. In addition, as discussed above, during the three months ended September 30, 2016, we recorded allowance charges of approximately \$94.0 million resulting from delays or shortfalls in collections against the forecasts for certain pools in Europe. These changes in forecasted future cash flows resulted in an increase in the aggregate total estimated remaining collections for the receivable portfolios of approximately \$296.5 million as of September 30, 2016. The increase in the collection forecast from 120 months to 180 months had the effect of reducing the allowance charges by approximately \$13.2 million. For portfolios in Europe that were not extended to 180 months, we will continue to include collection forecast to 120 months in calculating accretion revenue and in our estimated remaining collection disclosures. In the United States, we will continue to include collection forecast to 120 months in calculating accretion revenue. Expected collections beyond the 120 month collection forecast in the United States are included in our estimated remaining collection disclosures but are not included in the calculation of accretion revenue.

The following tables summarize collections, revenue, end of period receivable balance and other related supplemental data, by year of purchase (in thousands, except percentages):

|                     | Three Months Ended September 30, 2016 |                              |   |                                    |                            | As of<br>September 30, 2016 |             |  |  |
|---------------------|---------------------------------------|------------------------------|---|------------------------------------|----------------------------|-----------------------------|-------------|--|--|
|                     | Collections <sup>(1)</sup>            | Gross Revenue <sup>(2)</sup> | Revenue Recognition Rate <sup>(3)</sup> | Net Reversal (Portfolio Allowance) | Revenue % of Total Revenue | Unamortized Balances        | Monthly IRR |  |  |
| United States:      |                                       |                              |   |                                    |                            |                             |             |  |  |
| ZBA <sup>(4)</sup>  | \$38,164                              | \$36,528                     | 95.7 %                                  | \$1,674                            | 14.6 %                     | \$—                         | —           |  |  |
| 2007                | 580                                   | 173                          | 29.8 %                                  | 166                                | 0.1 %                      | 942                         | 4.6 %       |  |  |
| 2008                | 1,648                                 | 704                          | 42.7 %                                  | 724                                | 0.3 %                      | 3,631                       | 5.2 %       |  |  |
| 2009 <sup>(5)</sup> | —                                     | —                            | —                                       | —                                  | —                          | —                           | —           |  |  |
| 2010                | 2,397                                 | 1,760                        | 73.4 %                                  | —                                  | 0.7 %                      | 1,902                       | 25.0 %      |  |  |
| 2011                | 9,503                                 | 6,041                        | 63.6 %                                  | —                                  | 2.4 %                      | 9,237                       | 16.1 %      |  |  |
| 2012                | 25,960                                | 16,973                       | 65.4 %                                  | —                                  | 6.8 %                      | 46,288                      | 11.0 %      |  |  |
| 2013                | 43,940                                | 29,954                       | 68.2 %                                  | —                                  | 11.9 %                     | 102,270                     | 8.9 %       |  |  |
| 2014                | 48,860                                | 26,392                       | 54.0 %                                  | —                                  | 10.5 %                     | 205,503                     | 4.0 %       |  |  |
| 2015                | 51,548                                | 24,811                       | 48.1 %                                  | —                                  | 9.8 %                      | 341,126                     | 2.3 %       |  |  |
| 2016                | 33,013                                | 19,996                       | 60.6 %                                  | —                                  | 8.0 %                      | 384,603                     | 2.2 %       |  |  |
| Subtotal            | 255,613                               | 163,332                      | 63.9 %                                  | 2,564                              | 65.1 %                     | 1,095,502                   | 3.7 %       |  |  |
| Europe:             |                                       |                              |   |                                    |                            |                             |             |  |  |
| 2013                | 39,624                                | 26,925                       | 68.0 %                                  | (76,018 )                          | 10.7 %                     | 286,472                     | 3.0 %       |  |  |
| 2014                | 37,038                                | 21,869                       | 59.0 %                                  | (13,150 )                          | 8.7 %                      | 341,855                     | 2.1 %       |  |  |
| 2015                | 31,236                                | 14,886                       | 47.7 %                                  | (4,843 )                           | 5.9 %                      | 289,982                     | 1.6 %       |  |  |
| 2016                | 13,640                                | 7,933                        | 58.2 %                                  | —                                  | 3.2 %                      | 206,978                     | 1.5 %       |  |  |
| Subtotal            | 121,538                               | 71,613                       | 58.9 %                                  | (94,011 )                          | 28.5 %                     | 1,125,287                   | 2.1 %       |  |  |
| Other geographies:  |                                       |                              |   |                                    |                            |                             |             |  |  |
| ZBA <sup>(4)</sup>  | 1,770                                 | 1,789                        | 101.1 %                                 | —                                  | 0.7 %                      | —                           | —           |  |  |
| 2013                | 410                                   | —                            | 0.0 %                                   | —                                  | 0.0 %                      | 1,408                       | 0.0 %       |  |  |
| 2014                | 4,034                                 | 4,349                        | 107.8 %                                 | —                                  | 1.7 %                      | 61,055                      | 2.2 %       |  |  |
| 2015                | 14,203                                | 6,683                        | 47.1 %                                  | —                                  | 2.7 %                      | 61,125                      | 3.3 %       |  |  |
| 2016                | 9,393                                 | 3,215                        | 34.2 %                                  | —                                  | 1.3 %                      | 53,454                      | 2.1 %       |  |  |
| Subtotal            | 29,810                                | 16,036                       | 53.8 %                                  | —                                  | 6.4 %                      | 177,042                     | 2.7 %       |  |  |
| Total               | \$406,961                             | \$250,981                    | 61.7 %                                  | \$(91,447 )                        | 100.0 %                    | \$2,397,831                 | 2.9 %       |  |  |

(1) Does not include amounts collected on behalf of others.

(2) Gross revenue excludes the effects of net portfolio allowance or net portfolio allowance reversals.

(3) Revenue recognition rate excludes the effects of net portfolio allowance or net portfolio allowance reversals.

ZBA revenue typically has a 100% revenue recognition rate. However, collections on ZBA pool groups where a valuation allowance remains must first be recorded as an allowance reversal until the allowance for that pool group is zero. Once the entire valuation allowance is reversed, the revenue recognition rate will become 100%. ZBA gross revenue includes an immaterial amount of accounts that are returned to the seller in accordance with the respective purchase agreement (“Put-Backs”).

(5) Total collections realized exceed the net book value of the portfolio and have been converted to ZBA.

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|                           | Three Months Ended September 30, 2015 |                              |   |                                    |                            | As of September 30, 2015 |     |             |        |
|---------------------------|---------------------------------------|------------------------------|---|------------------------------------|----------------------------|--------------------------|-----|-------------|--------|
|                           | Collections <sup>(1)</sup>            | Gross Revenue <sup>(2)</sup> | Revenue Recognition Rate <sup>(3)</sup> | Net Reversal (Portfolio Allowance) | Revenue % of Total Revenue | Unamortized Balances     | IRR |             |        |
| United States:            |                                       |                              |   |                                    |                            |                          |     |             |        |
| ZBA <sup>(4)</sup>        | \$31,159                              | \$28,099                     | 90.2                                    | %                                  | \$ 3,097                   | 10.5                     | %   | \$—         | —      |
| 2007                      | 727                                   | 267                          | 36.7                                    | %                                  | 520                        | 0.1                      | %   | 1,797       | 4.6 %  |
| 2008                      | 3,259                                 | 2,016                        | 61.9                                    | %                                  | 1,444                      | 0.8                      | %   | 6,447       | 9.6 %  |
| 2009                      | 3,179                                 | 1,171                        | 36.8                                    | %                                  | —                          | 0.4                      | %   | 218         | 25.0 % |
| 2010                      | 5,015                                 | 3,072                        | 61.3                                    | %                                  | —                          | 1.1                      | %   | 4,373       | 18.8 % |
| 2011                      | 26,197                                | 19,754                       | 75.4                                    | %                                  | —                          | 7.3                      | %   | 32,871      | 17.3 % |
| 2012                      | 40,813                                | 25,190                       | 61.7                                    | %                                  | —                          | 9.4                      | %   | 92,866      | 8.0 %  |
| 2013                      | 67,986                                | 42,781                       | 62.9                                    | %                                  | —                          | 16.0                     | %   | 183,453     | 7.1 %  |
| 2014                      | 73,250                                | 36,418                       | 49.7                                    | %                                  | —                          | 13.5                     | %   | 325,382     | 3.5 %  |
| 2015                      | 32,917                                | 15,833                       | 48.1                                    | %                                  | —                          | 5.9                      | %   | 325,617     | 2.0 %  |
| Impact of CFPB settlement | —                                     | —                            |   |                                    | (8,322 )                   |                          |     | —           | —      |
| Subtotal                  | 284,502                               | 174,601                      | 61.4                                    | %                                  | (3,261 )                   | 65.0                     | %   | 973,024     | 5.5 %  |
| Europe:                   |                                       |                              |   |                                    |                            |                          |     |             |        |
| 2013                      | 51,210                                | 43,010                       | 84.0                                    | %                                  | —                          | 16.0                     | %   | 457,343     | 3.0 %  |
| 2014                      | 51,522                                | 30,362                       | 58.9                                    | %                                  | —                          | 11.3                     | %   | 473,135     | 2.1 %  |
| 2015                      | 26,024                                | 14,788                       | 56.8                                    | %                                  | —                          | 5.5                      | %   | 334,266     | 1.7 %  |
| Subtotal                  | 128,756                               | 88,160                       | 68.5                                    | %                                  | —                          | 32.8                     | %   | 1,264,744   | 2.3 %  |
| Other geographies:        |                                       |                              |   |                                    |                            |                          |     |             |        |
| ZBA <sup>(4)</sup>        | 646                                   | 646                          | 100.0                                   | %                                  | —                          | 0.2                      | %   | —           | —      |
| 2013                      | 2,181                                 | —                            | 0.0                                     | %                                  | —                          | 0.0                      | %   | 3,075       | 0.0 %  |
| 2014                      | 4,227                                 | 5,066                        | 119.8                                   | %                                  | —                          | 1.9                      | %   | 69,714      | 2.3 %  |
| 2015                      | 1,441                                 | 311                          | 21.6                                    | %                                  | —                          | 0.1                      | %   | 12,667      | 2.1 %  |
| Subtotal                  | 8,495                                 | 6,023                        | 70.9                                    | %                                  | —                          | 2.2                      | %   | 85,456      | 2.2 %  |
| Total                     | \$421,753                             | \$268,784                    | 63.7                                    | %                                  | \$ (3,261 )                | 100.0                    | %   | \$2,323,224 | 3.3 %  |

(1) Does not include amounts collected on behalf of others.

(2) Gross revenue excludes the effects of net portfolio allowance or net portfolio allowance reversals.

(3) Revenue recognition rate excludes the effects of net portfolio allowance or net portfolio allowance reversals.

ZBA revenue typically has a 100% revenue recognition rate. However, collections on ZBA pool groups where a valuation allowance remains must first be recorded as an allowance reversal until the allowance for that pool group is zero. Once the entire valuation allowance is reversed, the revenue recognition rate will become 100%. ZBA gross revenue includes an immaterial amount of Put-Backs.

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|                     | Nine Months Ended September 30, 2016 |                                 |   |   |   |                                  | As of<br>September 30, 2016 |                |
|---------------------|--------------------------------------|---------------------------------|---|---|---|----------------------------------|-----------------------------|----------------|
|                     | Collections <sup>(1)</sup>           | Gross<br>Revenue <sup>(2)</sup> | Revenue<br>Recognition<br>Rate <sup>(3)</sup> |   | Net<br>Reversal<br>(Portfolio<br>Allowance) | Revenue<br>% of Total<br>Revenue | Unamortized<br>Balances     | Monthly<br>IRR |
| United States:      |                                      |                                 |   |   |   |                                  |                             |                |
| ZBA <sup>(4)</sup>  | \$99,821                             | \$94,795                        | 95.0  | % | \$5,171                                     | 12.1                             | % \$—                       | —              |
| 2007                | 1,712                                | 587                             | 34.3  | % | 467   | 0.1                              | % 942                       | 4.6 %          |
| 2008                | 7,426                                | 3,663                           | 49.3  | % | 1,596                                       | 0.5                              | % 3,631                     | 5.2 %          |
| 2009 <sup>(5)</sup> | —                                    | —                               | —   |   | —   | —                                | —                           | —              |
| 2010                | 8,085                                | 6,270                           | 77.6  | % | —   | 0.8                              | % 1,902                     | 25.0 %         |
| 2011                | 48,941                               | 30,959                          | 63.3  | % | —   | 4.0                              | % 9,237                     | 16.1 %         |
| 2012                | 90,568                               | 57,582                          | 63.6  | % | —   | 7.3                              | % 46,288                    | 11.0 %         |
| 2013                | 158,446                              | 99,614                          | 62.9  | % | —   | 12.7                             | % 102,270                   | 8.9 %          |
| 2014                | 173,348                              | 87,854                          | 50.7  | % | —   | 11.2                             | % 205,503                   | 4.0 %          |
| 2015                | 180,200                              | 79,315                          | 44.0  | % | —   | 10.1                             | % 341,126                   | 2.3 %          |
| 2016                | 63,065                               | 34,720                          | 55.1  | % | —   | 4.4                              | % 384,603                   | 2.2 %          |
| Subtotal            | 831,612                              | 495,359                         | 59.6  | % | 7,234                                       | 63.2                             | % 1,095,502                 | 3.7 %          |
| Europe:             |                                      |                                 |   |   |   |                                  |                             |                |
| 2013                | 130,082                              | 103,342                         | 79.4  | % | (76,018 )                                   | 13.2                             | % 286,472                   | 3.0 %          |
| 2014                | 121,938                              | 73,747                          | 60.5  | % | (13,150 )                                   | 9.4                              | % 341,855                   | 2.1 %          |
| 2015                | 96,926                               | 49,540                          | 51.1  | % | (4,843 )                                    | 6.3                              | % 289,982                   | 1.6 %          |
| 2016                | 27,076                               | 15,420                          | 57.0  | % | —   | 2.0                              | % 206,978                   | 1.5 %          |
| Subtotal            | 376,022                              | 242,049                         | 64.4  | % | (94,011 )                                   | 30.9                             | % 1,125,287                 | 2.1 %          |
| Other geographies:  |                                      |                                 |   |   |   |                                  |                             |                |
| ZBA <sup>(4)</sup>  | 5,436                                | 5,309                           | 97.7  | % | —   | 0.7                              | % —                         | —              |
| 2013                | 1,204                                | —                               | 0.0   | % | —   | 0.0                              | % 1,408                     | 0.0 %          |
| 2014                | 13,398                               | 13,551                          | 101.1   | % | —   | 1.7                              | % 61,055                    | 2.2 %          |
| 2015                | 44,290                               | 21,512                          | 48.6  | % | —   | 2.7                              | % 61,125                    | 3.3 %          |
| 2016                | 16,904                               | 6,077                           | 36.0  | % | —   | 0.8                              | % 53,454                    | 2.1 %          |
| Subtotal            | 81,232                               | 46,449                          | 57.2  | % | —   | 5.9                              | % 177,042                   | 2.7 %          |
| Total               | \$1,288,866                          | \$783,857                       | 60.8  | % | \$(86,777 )                                 | 100.0                            | % \$2,397,831               | 2.9 %          |

(1) Does not include amounts collected on behalf of others.

(2) Gross revenue excludes the effects of net portfolio allowance or net portfolio allowance reversals.

(3) Revenue recognition rate excludes the effects of net portfolio allowance or net portfolio allowance reversals.

ZBA revenue typically has a 100% revenue recognition rate. However, collections on ZBA pool groups where a valuation allowance remains must first be recorded as an allowance reversal until the allowance for that pool group is zero. Once the entire valuation allowance is reversed, the revenue recognition rate will become 100%. ZBA gross revenue includes an immaterial amount of Put-Backs.

(5) Total collections realized exceed the net book value of the portfolio and have been converted to ZBA.

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|                           | Nine Months Ended September 30, 2015 |                              |   |                                    |                            | As of<br>September 30, 2015 |             |  |  |
|---------------------------|--------------------------------------|------------------------------|---|------------------------------------|----------------------------|-----------------------------|-------------|--|--|
|                           | Collections <sup>(1)</sup>           | Gross Revenue <sup>(2)</sup> | Revenue Recognition Rate <sup>(3)</sup> | Net Reversal (Portfolio Allowance) | Revenue % of Total Revenue | Unamortized Balances        | Monthly IRR |  |  |
| United States:            |                                      |                              |   |                                    |                            |                             |             |  |  |
| ZBA <sup>(4)</sup>        | \$72,342                             | \$63,042                     | 87.1 %                                  | \$9,509                            | 7.9 %                      | \$—                         | —           |  |  |
| 2007                      | 2,486                                | 872                          | 35.1 %                                  | 816                                | 0.1 %                      | 1,797                       | 4.6 %       |  |  |
| 2008                      | 10,471                               | 6,693                        | 63.9 %                                  | 1,955                              | 0.8 %                      | 6,447                       | 9.6 %       |  |  |
| 2009                      | 17,812                               | 10,293                       | 57.8 %                                  | —                                  | 1.3 %                      | 218                         | 25.0 %      |  |  |
| 2010                      | 39,358                               | 22,777                       | 57.9 %                                  | —                                  | 2.9 %                      | 4,373                       | 18.8 %      |  |  |
| 2011                      | 89,638                               | 67,889                       | 75.7 %                                  | —                                  | 8.5 %                      | 32,871                      | 17.3 %      |  |  |
| 2012                      | 141,648                              | 86,577                       | 61.1 %                                  | —                                  | 11.0 %                     | 92,866                      | 8.0 %       |  |  |
| 2013                      | 235,970                              | 137,742                      | 58.4 %                                  | —                                  | 17.3 %                     | 183,453                     | 7.1 %       |  |  |
| 2014                      | 239,737                              | 112,315                      | 46.8 %                                  | —                                  | 14.1 %                     | 325,382                     | 3.5 %       |  |  |
| 2015                      | 58,881                               | 24,935                       | 42.3 %                                  | —                                  | 3.1 %                      | 325,617                     | 2.0 %       |  |  |
| Impact of CFPB settlement | —                                    | —                            |   | (8,322)                            | —                          | —                           | —           |  |  |
| Subtotal                  | 908,343                              | 533,135                      | 58.7 %                                  | 3,958                              | 67.0 %                     | 973,024                     | 4.7 %       |  |  |
| Europe:                   |                                      |                              |   |                                    |                            |                             |             |  |  |
| 2013                      | 163,097                              | 130,345                      | 79.9 %                                  | —                                  | 16.4 %                     | 457,343                     | 3.0 %       |  |  |
| 2014                      | 153,043                              | 93,835                       | 61.3 %                                  | —                                  | 11.8 %                     | 473,135                     | 2.1 %       |  |  |
| 2015                      | 35,781                               | 20,716                       | 57.9 %                                  | —                                  | 2.6 %                      | 334,266                     | 1.7 %       |  |  |
| Subtotal                  | 351,921                              | 244,896                      | 69.6 %                                  | —                                  | 30.8 %                     | 1,264,744                   | 2.3 %       |  |  |
| Other geographies:        |                                      |                              |   |                                    |                            |                             |             |  |  |
| ZBA <sup>(4)</sup>        | 1,738                                | 1,738                        | 100.0 %                                 | —                                  | 0.2 %                      | —                           | —           |  |  |
| 2012                      | 471                                  | —                            | 0.0 %                                   | —                                  | 0.0 %                      | —                           | 0.0 %       |  |  |
| 2013                      | 7,122                                | 312                          | 4.4 %                                   | —                                  | 0.0 %                      | 3,075                       | 0.0 %       |  |  |
| 2014                      | 11,580                               | 15,180                       | 131.1 %                                 | —                                  | 1.9 %                      | 69,714                      | 2.3 %       |  |  |
| 2015                      | 2,973                                | 715                          | 24.0 %                                  | —                                  | 0.1 %                      | 12,667                      | 2.1 %       |  |  |
| Subtotal                  | 23,884                               | 17,945                       | 75.1 %                                  | —                                  | 2.2 %                      | 85,456                      | 2.2 %       |  |  |
| Total                     | \$1,284,148                          | \$795,976                    | 62.0 %                                  | \$3,958                            | 100.0 %                    | \$2,323,224                 | 3.3 %       |  |  |

(1) Does not include amounts collected on behalf of others.

(2) Gross revenue excludes the effects of net portfolio allowance or net portfolio allowance reversals.

(3) Revenue recognition rate excludes the effects of net portfolio allowance or net portfolio allowance reversals.

ZBA revenue typically has a 100% revenue recognition rate. However, collections on ZBA pool groups where a valuation allowance remains must first be recorded as an allowance reversal until the allowance for that pool group is zero. Once the entire valuation allowance is reversed, the revenue recognition rate will become 100%. ZBA gross revenue includes an immaterial amount of Put-Backs.

Other revenues were \$19.9 million and \$13.4 million for the three months ended September 30, 2016 and 2015, respectively, and \$60.8 million and \$39.4 million for the nine months ended September 30, 2016 and 2015, respectively. The increase in other revenues was primarily attributable to contingent fee income earned at our international subsidiaries, offset by the negative impact of foreign currency translation. Most of our other revenues are from our international subsidiaries and therefore, other revenues were unfavorably impacted by the strengthening of the U.S. dollar relative to other foreign currencies during the periods presented.

#### Operating Expenses

Total operating expenses were \$200.6 million during the three months ended September 30, 2016, a decrease of \$47.6 million, or 19.2%, compared to total operating expenses of \$248.2 million during the three months ended September 30,





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2015. Total operating expenses were \$603.8 million during the nine months ended September 30, 2016, a decrease of \$37.6 million, or 5.9%, compared to total operating expenses of \$641.4 million during the nine months ended September 30, 2015.

Operating expenses are explained in more detail as follows:

**Salaries and Employee Benefits**

Salaries and employee benefits increased \$4.8 million, or 7.6%, to \$67.8 million during the three months ended September 30, 2016, from \$63.0 million during the three months ended September 30, 2015. The increase was primarily the result of increases in headcount and related compensation expense of approximately \$9.0 million for our international subsidiaries, offset by a decrease of \$4.6 million in stock-based compensation expense.

Salaries and employee benefits increased \$18.8 million, or 9.7%, to \$212.9 million during the nine months ended September 30, 2016, from \$194.1 million during the nine months ended September 30, 2015. The increase was primarily the result of increases in headcount and related compensation expense of approximately \$31.4 million for our international subsidiaries, offset by a decrease of \$7.8 million in stock-based compensation expense and a net decrease in other salaries and employee benefits in our U.S. operations.

Stock-based compensation decreased \$4.6 million, or 87.7%, to \$0.6 million during the three months ended September 30, 2016, from \$5.2 million during the three months ended September 30, 2015. Stock-based compensation decreased \$7.8 million, or 44.9%, to \$9.5 million during the nine months ended September 30, 2016, from \$17.3 million during the nine months ended September 30, 2015. The decreases were primarily attributable to expense reversals resulting from adjustments to estimated vesting of certain performance-based awards and lower fair value of equity awards granted in recent periods.

**Cost of Legal Collections**

Cost of legal collections includes primarily contingent fees paid to our network of attorneys and the cost of litigation. We pursue legal collection using a network of attorneys that specialize in collection matters and through our internal legal channel. Under the agreements with our contracted attorneys, we advance certain out-of-pocket court costs, or Deferred Court Costs. We capitalize these costs in the consolidated financial statements and provide a reserve for those costs that we believe will ultimately be uncollectible. We determine the reserve based on an estimated court cost recovery rate based on our analysis of historical court costs recovery data. Based on recent trends of historical court costs recovery data, we noted a decrease in the estimated court cost recovery rate in the United Kingdom. Based on the revised estimated court cost recovery rate, we recorded an additional court costs reserve in the cost of legal collections of approximately \$11.3 million during the three months ended September 30, 2016.

During the three months ended September 30, 2016, overall cost of legal collections decreased \$1.9 million, or 3.1%, to \$56.9 million, as compared to \$58.8 million during the corresponding period in the prior year. Cost of legal collections in the United States decreased by \$14.2 million, or 26.8%, while cost of legal collections in Europe increased by \$12.5 million, or 216.9%, as compared to the corresponding period in the prior year. The cost of legal collections as a percentage of gross collections through this channel was 34.5% during the three months ended September 30, 2016, an increase from 32.9% during the corresponding period in 2015. The cost of legal collections as a percentage of gross collections through this channel in the United States was 29.6% and 34.4% during the three months ended September 30, 2016 and 2015, respectively. The cost of legal collections as a percentage of gross collections through this channel in Europe was 57.9% and 23.3% during the three months ended September 30, 2016 and 2015, respectively.

During the nine months ended September 30, 2016, overall cost of legal collections decreased \$12.8 million, or 7.5%, to \$158.0 million, as compared to \$170.8 million during the corresponding period in the prior year. Cost of legal collections in the United States decreased by \$28.9 million, or 19.0%, while cost of legal collections in Europe increased by \$14.9 million, or 81.1% as compared to the corresponding period in the prior year. The cost of legal collections as a percentage of gross collections through this channel was 29.8% during the nine months ended September 30, 2016, a decrease from 31.4% during the corresponding period in 2015. The cost of legal collections as a percentage of gross collections through this channel in the United States was 28.9% and 31.7% during the nine months ended September 30, 2016 and 2015, respectively. The cost of legal collections as a percentage of gross collections through this channel in Europe was 35.2% and 28.9% during the nine months ended September 30, 2016

and 2015, respectively.

The decreases in the cost of legal collections and the cost of legal collections as a percentage of gross collections through this channel in the United States during the periods presented were due to a reduction in upfront court costs as a result of fewer accounts placed in this channel because of temporary delays in receiving media from issuers required to initiate the legal process for a number of accounts as compared to the corresponding period in the prior year. We believe these temporary delays

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will decrease in the fourth quarter of 2016 and expect increased placements in our legal channel thereafter. The increases in cost of legal collections and the cost of legal collections as a percentage of gross collections through this channel in Europe during the periods presented were the result of the \$11.3 million additional court costs reserve as discussed above.

**Other Operating Expenses**

Other operating expenses increased by \$1.9 million, or 8.6%, to \$24.1 million during the three months ended September 30, 2016, from \$22.2 million during the three months ended September 30, 2015. Other operating expenses increased \$7.1 million, or 10.5%, to \$75.4 million during the nine months ended September 30, 2016, from \$68.3 million during the nine months ended September 30, 2015. The increase in other operating expenses for the nine months ended September 30, 2016, as compared to the prior period, was primarily due to increased costs relating to various operation support activities, including skip tracing, media requests and bank charges.

**Collection Agency Commissions**

During the three months ended September 30, 2016, we incurred \$8.8 million in commissions to third-party collection agencies, or 19.1% of the related gross collections of \$46.3 million. During the period, the commission rate as a percentage of related gross collections was 7.2% and 24.5% for our collection outsourcing channels in the United States and Europe, respectively. During the three months ended September 30, 2015, we incurred \$9.4 million in commissions, or 16.7%, of the related gross collections of \$56.0 million. During the period, the commission rate as a percentage of related gross collections was 13.3% and 18.8% for our collection outsourcing channels in the United States and Europe, respectively.

During the nine months ended September 30, 2016, we incurred \$28.2 million in commissions to third-party collection agencies, or 18.2% of the related gross collections of \$155.0 million. During the period, the commission rate as a percentage of related gross collections was 9.5% and 21.6% for our collection outsourcing channels in the United States and Europe, respectively. During the nine months ended September 30, 2015, we incurred \$28.5 million in commissions, or 17.2%, of the related gross collections of \$166.0 million. During the period, the commission rate as a percentage of related gross collections was 15.6% and 18.0% for our collection outsourcing channels in the United States and Europe, respectively.

Collections through this channel vary from period to period depending on, among other things, the number of accounts placed with an agency versus accounts collected internally. Commissions, as a percentage of collections in this channel also vary from period to period depending on, among other things, the amount of time that has passed since the charge-off of the accounts placed with an agency, the asset class, and the geographic location of the receivables. Generally, freshly charged-off accounts have a lower commission rate than accounts that have been charged off for a longer period of time. Additionally, commission rates are lower in the United Kingdom where most of the receivables in this channel are semi-performing loans and IVAs, while the commission rates are higher in other European countries where most of the receivables in this channel are non-performing loans.

**General and Administrative Expenses**

General and administrative expenses decreased \$51.9 million, or 59.8%, to \$34.9 million during the three months ended September 30, 2016, from \$86.8 million during the three months ended September 30, 2015. Excluding acquisition, integration and restructuring related expenses, and settlement fees and related administrative expenses of \$5.1 million and \$55.9 million during the three months ended September 30, 2016 and 2015, respectively, general and administrative expenses decreased by \$1.2 million, or 3.7%, to \$29.7 million during the three months ended September 30, 2016, from \$30.9 million during the three months ended September 30, 2015.

General and administrative expenses decreased \$52.6 million, or 33.8%, to \$103.0 million during the nine months ended September 30, 2016, from \$155.6 million during the nine months ended September 30, 2015. Excluding acquisition, integration and restructuring related expenses and settlement fees and related administrative expenses of \$12.3 million and \$68.0 million during the nine months ended September 30, 2016 and 2015, respectively, general and administrative expenses increased \$3.1 million, or 3.5%, to \$90.8 million during the nine months ended September 30, 2016, from \$87.7 million during the nine months ended September 30, 2015. The increase was primarily due to increased general and administrative expenses at our international subsidiaries.

**Depreciation and Amortization**

Depreciation and amortization expense was consistent at \$8.0 million during the three months ended September 30, 2016 and 2015. Depreciation and amortization expense increased \$2.0 million, or 8.6%, to \$26.1 million during the nine months ended September 30, 2016, from \$24.1 million during the nine months ended September 30, 2015. The increase was primarily attributable to additional depreciation and amortization expenses resulting from fixed assets and intangible assets acquired through our recent acquisitions.

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## Cost per Dollar Collected

We utilize adjusted operating expenses in order to facilitate a comparison of approximate cash costs to cash collections for our portfolio purchasing and recovery business. The calculation of adjusted operating expenses is illustrated in detail in the “Non-GAAP Disclosure” section. The following table summarizes our overall cost per dollar collected by geographic location during the periods presented:

|                                   | Three Months Ended |       | Nine Months Ended |       |
|-----------------------------------|--------------------|-------|-------------------|-------|
|                                   | September 30,      |       | September 30,     |       |
|                                   | 2016               | 2015  | 2016              | 2015  |
| United States                     | 41.0%              | 43.0% | 39.7%             | 41.4% |
| Europe                            | 40.3%              | 31.4% | 35.0%             | 31.6% |
| Other geographies                 | 44.1%              | 30.2% | 42.5%             | 29.2% |
| Overall cost per dollar collected | 41.1%              | 39.2% | 38.5%             | 38.5% |

Our overall cost per dollar collected (or “cost-to-collect”) for the three months ended September 30, 2016 was 41.1%, up 190 basis points from 39.2% during the prior period. Overall cost-to-collect remained consistent at 38.5% during the nine months ended September 30, 2016 as compared to the corresponding period in the prior year. The increase in overall cost-to-collect during the three months ended September 30, 2016, as compared to the corresponding period in the prior year, was primarily due to increased cost-to-collect in Europe, offset by improved cost-to-collect in the United States. The steep increase in cost-to-collect in Europe was primarily due to the recording of approximately \$11.3 million additional court costs reserve in the United Kingdom during the three months ended September 30, 2016. To counter higher prices in the U.S. market, we implemented innovative consumer-centric programs aimed at increasing liquidations. These programs were initiated in the beginning of 2014 and have become increasingly successful. As we continue to grow our presence in the Latin American market, we expect to incur upfront cost in building our collection channels. As a result, cost-to-collect in this region may become elevated in the near term and may fluctuate over time.

Over time, we expect our cost-to-collect to remain competitive, but also to fluctuate from quarter to quarter based on seasonality, acquisitions, the cost of investments in new operating initiatives, and the changing regulatory and legislative environment.

## Interest Expense

Interest expense increased \$0.8 million to \$48.6 million during the three months ended September 30, 2016, from \$47.8 million during the three months ended September 30, 2015. Interest expense increased \$13.5 million to \$149.9 million during the nine months ended September 30, 2016, from \$136.4 million during the nine months ended September 30, 2015.

The following tables summarize our interest expense (in thousands):

|   | Three Months Ended              |           |           |
|---|---------------------------------|-----------|-----------|
|   | September 30,                   |           |           |
|   | 2016                            | 2015      | \$ Change |
| Stated interest on debt obligations               | \$39,494                        | \$39,466  | \$ 28     |
| Interest expense on preferred equity certificates | 5,903                           | 6,254     | (351 )    |
| Amortization of loan fees and other loan costs    | 3,157                           | 2,508     | 649       |
| Amortization of debt discount                     | 2,620                           | 2,359     | 261       |
| Accretion of debt premium                         | (2,542 )                        | (2,771 )  | 229       |
| Total interest expense                            | \$48,632                        | \$47,816  | \$ 816    |
|   | Nine Months Ended September 30, |           |           |
|   | 2016                            | 2015      | \$ Change |
| Stated interest on debt obligations               | \$122,004                       | \$110,802 | \$ 11,202 |
| Interest expense on preferred equity certificates | 18,684                          | 18,360    | 324       |

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|  |           |           |          |
|--|-----------|-----------|----------|
| Amortization of loan fees and other loan costs | 9,217     | 8,238     | 979      |
| Amortization of debt discount                  | 7,869     | 6,947     | 922      |
| Accretion of debt premium                      | (7,854 )  | (7,978 )  | 124      |
| Total interest expense                         | \$149,920 | \$136,369 | \$13,551 |

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The payment of the accumulated interest on the preferred equity certificates issued in connection with the acquisition of a controlling interest in Cabot will only be satisfied in connection with the disposition of the noncontrolling interests of J.C. Flowers & Co. LLC and management.

The increase in interest expense during the three months ended September 30, 2016 as compared to the corresponding period in 2015 was primarily attributable to interest expense recognized at Baycorp, which was acquired in October 2015. The increase in interest expense during the nine months ended September 30, 2016 as compared to the corresponding period in 2015 was primarily attributable to increased average debt levels in the United States and Europe and interest expense recognized at Baycorp.

**Other Income (Expense)**

Other income or expense consists primarily of foreign currency exchange gains or losses and interest income. Other income was \$4.1 million during the three months ended September 30, 2016, up from other expense of \$0.9 million during the three months ended September 30, 2015. Other income was \$14.4 million during the nine months ended September 30, 2016, up from \$1.6 million during the nine months ended September 30, 2015. The increases during the periods presented were primarily due to net gains recognized on foreign exchange contracts.

In 2016, Encore and its Cabot subsidiary collectively began entering into currency exchange forward contracts to reduce the effects of currency exchange rate fluctuations between the British Pound and Euro. These derivative contracts generally mature within one to three months and are not designated as hedge instruments for accounting purposes. The gains or losses on these derivative contracts are recognized in other income or expense based on the changes in fair value. Before the effect of income tax and noncontrolling interest, the net gain on these derivative contracts recognized in our condensed consolidated statements of operations was \$3.3 million and \$10.7 million during the three and nine months ended September 30, 2016, respectively.

**Income Taxes**

We recorded income tax benefits for loss from continuing operations of \$13.8 million and \$6.4 million, during the three months ended September 30, 2016 and 2015, respectively. We recorded income tax provisions for income from continuing operations of \$9.8 million and \$23.2 million, during the nine months ended September 30, 2016 and 2015, respectively.

The effective tax rates for the respective periods are shown below:

|  | Three Months<br>Ended<br>September 30,<br>2016 |         | Nine Months<br>Ended<br>September 30,<br>2015 |         |
|--|--|---------|---|---------|
| Federal (benefit) provision                      | (35.0)%  | (35.0)% | 35.0 %  | 35.0 %  |
| State (benefit) provision                        | (2.2 )%  | (2.4 )% | 2.2 %   | 2.4 %   |
| International provision (benefit) <sup>(1)</sup> | 16.0 %   | (20.5)% | 19.3 %  | (8.3 )% |
| Permanent items <sup>(2)</sup>                   | 0.3 %  | 1.4 %   | 3.3 %   | 1.2 %   |
| Tax effect of CFPB / regulatory charges          | 0.0 %  | 21.9 %  | 0.0 %   | 6.2 %   |
| Other <sup>(3)</sup>                             | (0.1 )%  | (0.7 )% | (6.7)%  | 0.2 %   |
| Effective rate                                   | (21.0)%  | (35.3)% | 53.1 %  | 36.7 %  |

(1)Relates primarily to lower tax rates on income or loss attributable to international operations.

(2)Represents a provision for nondeductible items.

(3)Includes the effect of discrete items and an IRS audit settlement.

Our effective tax rate could fluctuate significantly on a quarterly basis and could be adversely affected to the extent earnings are lower than anticipated in countries that have lower statutory tax rates and higher than anticipated in countries that have higher statutory tax rates.

The effective tax rates fluctuated significantly during the periods presented due to the following factors.

In accordance with the authoritative guidance for income taxes, each interim period is considered an integral part of the annual period and tax expense or benefit is measured using an estimated annual effective income tax rate. The estimated annual





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effective income tax rate for the full year is applied to the respective interim period, taking into account year-to-date amounts and projected amounts for the year. Since we operate in foreign countries with varying tax rates that are much lower than the tax rate in the United States, the magnitude of the impact of the results from the international operations have on our quarterly effective tax rate is dependent on the level of income or loss from the international operations in the period. During the third quarter, we recorded a large allowance charge on certain portfolio pool groups in Europe and incurred pre-tax losses. As required under the authoritative guidance for interim tax reporting, we considered this loss and the related tax benefit in determining our estimated tax rate for the year, which is then applied to our third quarter pre-tax results in determining our tax expense. Since the loss is tax effected at a much lower tax rate in the United Kingdom, which results in lower tax benefit; and the income in the United States is taxed at a much higher tax rate, which results in higher tax expense, the loss has the effect of increasing our estimated annual tax rate significantly. Additionally, since the tax rate expected for the year will also be much higher due to the aforementioned factors, we expect that our tax expense in the fourth quarter will likely exceed tax expense that would normally be expected by approximately \$10 million.

Our subsidiary in Costa Rica is operating under a 100% tax holiday through December 31, 2018 and a 50% tax holiday for the subsequent four years. The impact of the tax holiday in Costa Rica for the three and nine months ended September 30, 2016 and 2015 was immaterial.

**Non-GAAP Disclosure**

In addition to the financial information prepared in conformity with Generally Accepted Accounting Principles (“GAAP”), we provide historical non-GAAP financial information. Management believes that the presentation of such non-GAAP financial information is meaningful and useful in understanding the activities and business metrics of our operations. Management believes that these non-GAAP financial measures reflect an additional way of viewing aspects of our business that, when viewed with our GAAP results, provide a more complete understanding of factors and trends affecting our business.

Management believes that the presentation of these measures provides investors with greater transparency and facilitates comparison of operating results across a broad spectrum of companies with varying capital structures, compensation strategies, derivative instruments, and amortization methods, which provide a more complete understanding of our financial performance, competitive position, and prospects for the future. Readers should consider the information in addition to, but not instead of, our financial statements prepared in accordance with GAAP. This non-GAAP financial information may be determined or calculated differently by other companies, limiting the usefulness of these measures for comparative purposes.

**Adjusted Income From Continuing Operations Per Share.** Management uses non-GAAP adjusted income from continuing operations attributable to Encore and adjusted income from continuing operations per share (which we also refer to from time to time as adjusted earnings per share), to assess operating performance, in order to highlight trends in our business that may not otherwise be apparent when relying on financial measures calculated in accordance with GAAP. Adjusted income from continuing operations attributable to Encore excludes non-cash interest and issuance cost amortization relating to our convertible notes, one-time charges, acquisition, integration and restructuring related expenses, settlement fees and related administrative expenses, and amortization of certain acquired intangible assets. The following table provides a reconciliation between income (loss) from continuing operations and diluted income (loss) from continuing operations per share attributable to Encore calculated in accordance with GAAP to adjusted income from continuing operations and adjusted income from continuing operations per share attributable to Encore, respectively. GAAP diluted earnings per share for the nine months ended September 30, 2015, includes the effect of approximately 0.8 million common shares, that are issuable upon conversion of certain convertible senior notes because the average stock price during the period exceeded the conversion price of these notes. However, as described in Note 10, “Debt—Encore Convertible Notes,” in the notes to our condensed consolidated financial statements, we have certain hedging transactions in place that have the effect of increasing the effective conversion price of these notes. Accordingly, while these common shares are included in our diluted earnings per share, the hedge transactions will offset the impact of this dilution and no shares will be issued unless our stock price exceeds the effective conversion price, thereby creating a discrepancy between the accounting effect of those notes under GAAP and their economic impact.

Because we reported GAAP net loss from continuing operations attributed to Encore during the three months ended September 30, 2016 and 2015, the shares used to calculate GAAP net loss per diluted share - accounting and GAAP net loss per diluted share - economic during the periods exclude dilutive potential common shares because of their anti-dilutive effect. After the non-GAAP adjustments however, we reported non-GAAP adjusted income from continuing operations attributable to Encore, the shares used to calculate non-GAAP adjusted income from continuing operations attributable to Encore per share, both accounting and economic, were approximately 25,911,000 during the three months ended September 30, 2016. During the three months ended September 30, 2015 accounting and economic shares were approximately 26,507,000 and 25,679,000, respectively.

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We have presented the following metrics both including and excluding the dilutive effect of these convertible senior notes to better illustrate the economic impact of those notes and the related hedging transactions to shareholders, with the GAAP item under the “Per Diluted Share-Accounting” and “Per Diluted Share-Economic” (non-GAAP) columns, respectively (in thousands, except per share data):

|  | Three Months Ended September 30, |             |            |            |             |            |
|--|----------------------------------|-------------|------------|------------|-------------|------------|
|  | 2016                             | Per Diluted |            | 2015       | Per Diluted |            |
|  | \$                               | Share—      | Share—     | \$         | Share—      | Share—     |
|  |                                  | Accounting  | Economic   |            | Accounting  | Economic   |
| GAAP net loss from continuing operations attributable to Encore, as reported               | \$(1,524)                        | \$ (0.06 )  | \$ (0.06 ) | \$(13,245) | \$ (0.52 )  | \$ (0.52 ) |
| Effect of diluted potential shares excluded from loss per share calculation <sup>(1)</sup> | —                                | —           | —          | —          | 0.01        | 0.01       |
| Adjustments:   |                                  |             |            |            |             |            |
| Convertible notes non-cash interest and issuance cost amortization                         | 2,983                            | 0.12        | 0.12       | 2,859      | 0.11        | 0.11       |
| Acquisition, integration and restructuring related expenses                                | 3,843                            | 0.15        | 0.15       | 2,235      | 0.09        | 0.09       |
| Settlement fees and related administrative expenses <sup>(2)</sup>                         | 2,613                            | 0.10        | 0.10       | 63,019     | 2.38        | 2.45       |
| Amortization of certain acquired intangible assets <sup>(3)</sup>                          | 529                              | 0.02        | 0.02       | —          | —           | —          |
| Income tax effect of the adjustments <sup>(4)</sup>  | (3,263 )                         | (0.13 )     | (0.13 )    | (22,268 )  | (0.84 )     | (0.87 )    |
| Adjustments attributable to noncontrolling interest <sup>(5)</sup>                         | (1,568 )                         | (0.06 )     | (0.06 )    | (418 )     | (0.02 )     | (0.02 )    |
| Adjusted income from continuing operations attributable to Encore                          | \$3,613                          | \$ 0.14     | \$ 0.14    | \$32,182   | \$ 1.21     | \$ 1.25    |

The shares used to calculate GAAP net loss per diluted share - accounting and GAAP net loss per diluted share - economic during the three months ended September 30, 2016 and 2015 exclude dilutive potential common shares because of their anti-dilutive effect.

Amount represents litigation and government settlement fees and related administrative expenses. For the three and nine months ended September 30, 2016 amounts consist of settlement and administrative fees related to certain TCPA settlements. For the three and nine months ended September 30, 2015, amounts relate to the consent order with the CFPB that we entered into in September 2015. We believe these fees and expenses are not indicative of ongoing operations and adjusting for these fees and expenses makes it easier to compare to prior periods, anticipated future periods, and our competitors' results.

As we continue to acquire debt solution service providers around the world, the acquired intangible assets, such as trade names and customer relationships, have grown substantially, particularly in recent quarters. These intangible assets are valued at the time of the acquisition and amortized over their estimated lives. We believe that amortization of acquisition-related intangible assets, especially the amortization of an acquired company's trade names and customer relationships, is the result of pre-acquisition activities. In addition, the amortization of these acquired intangibles is a non-cash static expense that is not affected by operations during any reporting period. As a result, the amortization of certain acquired intangible assets is excluded from our adjusted income from continuing operations attributable to Encore and adjusted income from continuing operations per share.

Amount represents the total income tax effect of the adjustments, which is calculated based on the applicable marginal tax rate of the jurisdiction in which the portion of the adjustment occurred.

Certain of the above pre-tax adjustments include expenses recognized by our partially-owned subsidiaries. This adjustment represents the portion of the non-GAAP adjustments that are attributable to noncontrolling interest.



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|  | Nine Months Ended September 30, |                                     |                                   |           |                                     |                                   |
|--|---------------------------------|-------------------------------------|-----------------------------------|-----------|-------------------------------------|-----------------------------------|
|  | 2016                            | 2015                                |                                   |           |                                     |                                   |
|  | \$                              | Per Diluted<br>Share—<br>Accounting | Per Diluted<br>Share—<br>Economic | \$        | Per Diluted<br>Share—<br>Accounting | Per Diluted<br>Share—<br>Economic |
| GAAP net income from continuing operations attributable to Encore, as reported | \$56,940                        | \$ 2.20                             | \$ 2.20                           | \$40,296  | \$ 1.50                             | \$ 1.55                           |
| Adjustments:   |                                 |                                     |                                   |           |                                     |                                   |
| Convertible notes non-cash interest and issuance cost amortization             | 8,813                           | 0.34                                | 0.34                              | 8,445     | 0.31                                | 0.32                              |
| Acquisition, integration and restructuring related expenses                    | 10,173                          | 0.39                                | 0.39                              | 14,298    | 0.54                                | 0.55                              |
| Settlement fees and related administrative expenses <sup>(2)</sup>             | 6,299                           | 0.24                                | 0.24                              | 63,019    | 2.34                                | 2.42                              |
| Amortization of certain acquired intangible assets <sup>(3)</sup>              | 2,178                           | 0.08                                | 0.08                              | —         | —                                   | —                                 |
| Income tax effect of the adjustments <sup>(4)</sup>                            | (8,884 )                        | (0.34 )                             | (0.34 )                           | (26,827 ) | (1.00 )                             | (1.03 )                           |
| Adjustments attributable to noncontrolling interest <sup>(5)</sup>             | (4,059 )                        | (0.15 )                             | (0.15 )                           | (4,981 )  | (0.19 )                             | (0.19 )                           |
| Adjusted income from continuing operations attributable to Encore              | \$71,460                        | \$ 2.76                             | \$ 2.76                           | \$94,250  | \$ 3.50                             | \$ 3.62                           |

The shares used to calculate GAAP net loss per diluted share - accounting and GAAP net loss per diluted share - (1) economic during the three months ended September 30, 2016 and 2015 exclude dilutive potential common shares because of their anti-dilutive effect.

Amount represents litigation and government settlement fees and related administrative expenses. For the three and nine months ended September 30, 2016 amounts consist of settlement and administrative fees related to certain TCPA settlements. For the three and nine months ended September 30, 2015, amounts relate to the consent order (2) with the CFPB that we entered into in September 2015. We believe these fees and expenses are not indicative of ongoing operations and adjusting for these fees and expenses makes it easier to compare to prior periods, anticipated future periods, and our competitors' results.

As we continue to acquire debt solution service providers around the world, the acquired intangible assets, such as trade names and customer relationships, have grown substantially, particularly in recent quarters. These intangible assets are valued at the time of the acquisition and amortized over their estimated lives. We believe that (3) amortization of acquisition-related intangible assets, especially the amortization of an acquired company's trade names and customer relationships, is the result of pre-acquisition activities. In addition, the amortization of these acquired intangibles is a non-cash static expense that is not affected by operations during any reporting period. As a result, the amortization of certain acquired intangible assets is excluded from our adjusted income from continuing operations attributable to Encore and adjusted income from continuing operations per share.

Amount represents the total income tax effect of the adjustments, which is calculated based on the applicable (4) marginal tax rate of the jurisdiction in which the portion of the adjustment occurred.

Certain of the above pre-tax adjustments include expenses recognized by our partially-owned subsidiaries. This (5) adjustment represents the portion of the non-GAAP adjustments that are attributable to noncontrolling interest.

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Adjusted EBITDA. Management utilizes adjusted EBITDA (defined as net income before discontinued operations, interest, taxes, depreciation and amortization, portfolio amortization, stock-based compensation expenses, one-time charges, acquisition, integration and restructuring related expenses, and settlement fees and related administrative expenses), which is materially similar in calculation to a financial measure contained in covenants used in the Encore revolving credit and term loan facility, in the evaluation of our operations and believes that this measure is a useful indicator of our ability to generate cash collections in excess of operating expenses through the liquidation of our receivable portfolios. Adjusted EBITDA for the periods presented is as follows (in thousands):

|   | Three Months Ended |            | Nine Months Ended |           |
|---|--------------------|------------|-------------------|-----------|
|   | September 30,      |            | September 30,     |           |
|   | 2016               | 2015       | 2016              | 2015      |
| GAAP net (loss) income, as reported                                 | \$(51,946 )        | \$(9,364 ) | \$5,494           | \$45,788  |
| Adjustments:  |                    |            |                   |           |
| (Income) loss from discontinued operations, net of tax              | —                  | (2,286 )   | 3,182             | (5,827 )  |
| Interest expense  | 48,632             | 47,816     | 149,920           | 136,369   |
| (Benefit) provision for income taxes                                | (13,768 )          | (6,361 )   | 9,831             | 23,174    |
| Depreciation and amortization                                       | 8,032              | 8,043      | 26,128            | 24,058    |
| Amount applied to principal on receivable portfolios <sup>(1)</sup> | 247,427            | 156,229    | 591,786           | 484,214   |
| Stock-based compensation expense                                    | 633                | 5,156      | 9,502             | 17,259    |
| Acquisition, integration and restructuring related expenses         | 3,843              | 2,235      | 9,255             | 12,893    |
| Settlement fees and related administrative expenses <sup>(2)</sup>  | 2,613              | 63,019     | 6,299             | 63,019    |
| Adjusted EBITDA   | \$245,466          | \$264,487  | \$811,397         | \$800,947 |

Amount represents collections from receivable portfolios that are not included in consolidated revenues as a result of accounting principles that require the application of such collections to amortize the principal of such receivable portfolios. We adjust for this amount because (a) the method is materially consistent with the calculation method (1) contained in covenants used in our revolving credit and term loan facility and (b) it represents actual cash collections and we believe this measure is a useful indicator of our ability to generate cash collections in excess of operating expenses through the liquidation of our receivable portfolios.

Amount represents litigation and government settlement fees and related administrative expenses. For the three and nine months ended September 30, 2016 amount consists of settlement and administrative fees related to certain TCPA settlements. For the three and nine months ended September 30, 2015, amount relates to the consent order (2) with the CFPB that we entered into in September 2015. We believe these fees and expenses are not indicative of ongoing operations and adjusting for these fees and expenses makes it easier to compare to prior periods, anticipated future periods, and our competitors' results. Adjusting for these settlement and administrative fees is materially consistent with the calculation method contained in covenants used in our revolving credit and term loan facility.

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Adjusted Operating Expenses. Management utilizes adjusted operating expenses in order to facilitate a comparison of approximate cash costs to cash collections for our portfolio purchasing and recovery business. Adjusted operating expenses for our portfolio purchasing and recovery business are calculated by starting with GAAP total operating expenses and backing out stock-based compensation expense, operating expenses related to non-portfolio purchasing and recovery business, one-time charges, acquisition, integration and restructuring related operating expenses, and settlement fees and related administrative expenses. Adjusted operating expenses related to our portfolio purchasing and recovery business for the periods presented are as follows (in thousands):

|   | Three Months Ended<br>September 30, |           | Nine Months Ended<br>September 30, |           |
|---|-------------------------------------|-----------|------------------------------------|-----------|
|   | 2016                                | 2015      | 2016                               | 2015      |
| GAAP total operating expenses, as reported  | \$200,597                           | \$248,185 | \$603,805                          | \$641,442 |
| Adjustments:  |                                     |           |                                    |           |
| Stock-based compensation expense  | (633 )                              | (5,156 )  | (9,502 )                           | (17,259 ) |
| Operating expenses related to non-portfolio purchasing and recovery business <sup>(1)</sup> | (26,446 )                           | (20,835 ) | (81,584 )                          | (62,404 ) |
| Acquisition, integration and restructuring related expenses                                 | (3,843 )                            | (2,235 )  | (10,173 )                          | (12,893 ) |
| Settlement fees and related administrative expenses <sup>(2)</sup>                          | (2,613 )                            | (54,697 ) | (6,299 )                           | (54,697 ) |
| Adjusted operating expenses related to portfolio purchasing and recovery business           | \$167,062                           | \$165,262 | \$496,247                          | \$494,189 |

Operating expenses related to non-portfolio purchasing and recovery business include operating expenses from (1) other operating segments that primarily engage in fee-based business, as well as corporate overhead not related to our portfolio purchasing and recovery business.

Amount represents litigation and government settlement fees and related administrative expenses. For the three and nine months ended September 30, 2016 amount consists of settlement and administrative fees related to certain TCPA settlements. For the three and nine months ended September 30, 2015, amount relates to the consent order with the CFPB that we entered into in September 2015. We believe these fees and expenses are not indicative of (2) ongoing operations and adjusting for these fees and expenses makes it easier to compare to prior periods, anticipated future periods, and our competitors' results. Adjusting for these settlement and administrative fees is materially consistent with the calculation method contained in covenants used in our revolving credit and term loan facility.

Supplemental Performance Data

The tables included in this supplemental performance data section include detail for purchases, collections and estimated remaining collections ("ERC") by year of purchase. During any fiscal quarter in which we acquire an entity that has portfolio, the entire historical portfolio of the acquired company is aggregated into static pools for the quarter of acquisition based on common characteristics, resulting in pools for that quarter that may consist of several different vintages of portfolio. These quarterly pools are included in the tables in this section by year of purchase. For example, with the acquisition of Cabot in July 2013, all of Cabot's historical portfolio to the date of the acquisition (which includes several years of historical purchases at various stages of maturity) is included in 2013 for Europe. Additional examples include, but are not limited to, the acquisition of Marlin in 2014 and the acquisition of dlc in 2015. Our collection expectations are based on demographic data, account characteristics, and economic variables. Additional adjustments are made to account for qualitative factors that may affect the payment behavior of our consumers and servicing related adjustments to ensure our collection expectations are aligned with our operations. Our collection expectations vary between types of portfolio and geographic location. For example, in the U.K., due to the higher concentration of payment plans, as compared to the U.S. and other locations in Europe, we expect to receive streams of collections over longer periods of time. As a result, past performance of pools in certain geographic locations or of certain types of portfolio are not necessarily a suitable indicator of future results in other locations or for other types of portfolio.



The supplemental performance data presented in this section is impacted by foreign currency translation, which represents the effect of translating financial results where the functional currency of our foreign subsidiary is different than our U.S. dollar reporting currency. For example, the strengthening of the U.S. dollar relative to other foreign currencies has an unfavorable reporting impact on our international purchases, collections, and ERC, and the weakening of the U.S. dollar relative to other foreign currencies has a favorable impact on our international purchases, collections, and ERC.

We utilize proprietary forecasting models to continuously evaluate the economic life of each pool.

During the quarter ended September 30, 2016, we revised the forecasting methodology we use to value and calculate IRRs on certain portfolios in Europe by extending the collection forecast from 120 months to 180 months. This change was

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made as a result of (1) our observation that older portfolios in Europe have consistently experienced cash collections beyond 120 months, (2) an expectation that regulatory changes in the United Kingdom resulting in a reduction in the number of highly discounted near term one-time settlements, an increase in the number of payment plans, and an increase in the length of existing payment plans will cause a lengthening of our collections curve, (3) an expectation that, as a result of a higher percentage of semi-performing account purchases in the United Kingdom in recent years, newer vintages will have a larger percentage of collections after 120 months and (4) our increased confidence in our ability to forecast future cash collections to 180 months. The increase in the collection forecast from 120 months to 180 months was applied effective July 1, 2016, to certain portfolios in Europe for which we could accurately forecast through such term. For portfolios in Europe that were not extended to 180 months, we will continue to include collection forecast to 120 months in calculating accretion revenue and in our estimated remaining collection disclosures. In the United States, we will continue to include collection forecast to 120 months in calculating accretion revenue. Expected collections beyond the 120 month collection forecast in the United States are included in our estimated remaining collection disclosures but are not included in the calculation of accretion revenue.

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## Cumulative Collections to Purchase Price Multiple

The following table summarizes our purchases and related gross collections by year of purchase (in thousands, except multiples):

| Year of Purchase                       | Purchase Price <sup>(1)</sup> | Cumulative Collections through September 30, 2016 |           |           |           |           |           |           |             |             |             |
|--|-------------------------------|---|-----------|-----------|-----------|-----------|-----------|-----------|-------------|-------------|-------------|
|  |                               | <2007   | 2007      | 2008      | 2009      | 2010      | 2011      | 2012      | 2013        | 2014        | 2015        |
| Purchased consumer receivables:        |                               |   |           |           |           |           |           |           |             |             |             |
| United States:                         |                               |   |           |           |           |           |           |           |             |             |             |
| <2007                                  | \$719,081                     | \$1,377,276                                       | \$286,676 | \$183,982 | \$114,648 | \$73,397  | \$52,137  | \$36,955  | \$28,242    | \$22,012    | \$17,000    |
| 2007                                   | 204,063                       | —   | 68,048    | 145,272   | 111,117   | 70,572    | 44,035    | 29,619    | 20,812      | 14,431      | 12,000      |
| 2008                                   | 227,753                       | —   | —         | 69,049    | 165,164   | 127,799   | 87,850    | 59,507    | 41,773      | 29,776      | 23,000      |
| 2009                                   | 252,988                       | —   | —         | —         | 96,529    | 206,773   | 164,605   | 111,569   | 80,443      | 58,345      | 42,000      |
| 2010                                   | 345,401                       | —   | —         | —         | —         | 125,465   | 284,541   | 215,088   | 150,558     | 106,079     | 80,000      |
| 2011                                   | 383,637                       | —   | —         | —         | —         | —         | 122,224   | 300,536   | 225,451     | 154,847     | 111,000     |
| 2012                                   | 466,559                       | —   | —         | —         | —         | —         | —         | 186,472   | 319,114     | 233,045     | 151,000     |
| 2013                                   | 512,897                       | —   | —         | —         | —         | —         | —         | —         | 217,245     | 372,967     | 271,000     |
| 2014                                   | 519,221                       | —   | —         | —         | —         | —         | —         | —         | —           | 144,178     | 301,000     |
| 2015                                   | 477,528                       | —   | —         | —         | —         | —         | —         | —         | —           | —           | 101,000     |
| 2016                                   | 378,369                       | —   | —         | —         | —         | —         | —         | —         | —           | —           | —           |
| Subtotal                               | 4,487,497                     | 1,377,276   | 354,724   | 398,303   | 487,458   | 604,006   | 755,392   | 939,746   | 1,083,638   | 1,135,680   | 1,135,680   |
| Europe:                                |                               |   |           |           |           |           |           |           |             |             |             |
| 2013                                   | 619,079                       | —   | —         | —         | —         | —         | —         | —         | 134,259     | 249,307     | 211,000     |
| 2014                                   | 630,343                       | —   | —         | —         | —         | —         | —         | —         | —           | 135,549     | 191,000     |
| 2015                                   | 423,359                       | —   | —         | —         | —         | —         | —         | —         | —           | —           | 65,000      |
| 2016                                   | 222,361                       | —   | —         | —         | —         | —         | —         | —         | —           | —           | —           |
| Subtotal                               | 1,895,142                     | —   | —         | —         | —         | —         | —         | —         | 134,259     | 384,856     | 477,000     |
| Other geographies:                     |                               |   |           |           |           |           |           |           |             |             |             |
| 2012                                   | 6,706                         | —   | —         | —         | —         | —         | —         | —         | 3,848       | 2,561       | 1,200       |
| 2013                                   | 29,568                        | —   | —         | —         | —         | —         | —         | —         | 6,617       | 17,615      | 10,000      |
| 2014                                   | 88,227                        | —   | —         | —         | —         | —         | —         | —         | —           | 9,652       | 16,000      |
| 2015                                   | 91,290                        | —   | —         | —         | —         | —         | —         | —         | —           | —           | 15,000      |
| 2016                                   | 60,627                        | —   | —         | —         | —         | —         | —         | —         | —           | —           | —           |
| Subtotal                               | 276,418                       | —   | —         | —         | —         | —         | —         | —         | 10,465      | 29,828      | 42,000      |
| Purchased U.S. bankruptcy receivables: |                               |   |           |           |           |           |           |           |             |             |             |
| 2010                                   | 11,971                        | —   | —         | —         | —         | 388       | 4,247     | 5,598     | 6,248       | 5,914       | 3,500       |
| 2011                                   | 1,642                         | —   | —         | —         | —         | —         | 1,372     | 1,413     | 1,070       | 333         | 24,000      |
| 2012                                   | 82,674                        | —   | —         | —         | —         | —         | —         | 1,249     | 31,020      | 26,207      | 21,000      |
| 2013                                   | 39,833                        | —   | —         | —         | —         | —         | —         | —         | 12,806      | 24,679      | 21,000      |
| 2014                                   | —                             | —   | —         | —         | —         | —         | —         | —         | —           | —           | —           |
| 2015                                   | 24,372                        | —   | —         | —         | —         | —         | —         | —         | —           | —           | 22,000      |
| 2016                                   | 33,777                        | —   | —         | —         | —         | —         | —         | —         | —           | —           | —           |
| Subtotal                               | 194,269                       | —   | —         | —         | —         | 388       | 5,619     | 8,260     | 51,144      | 57,133      | 46,000      |
| Total                                  | \$6,853,326                   | \$1,377,276                                       | \$354,724 | \$398,303 | \$487,458 | \$604,394 | \$761,011 | \$948,006 | \$1,279,506 | \$1,607,497 | \$1,607,497 |

(1) Adjusted for Put-Backs and Recalls. Recalls represent accounts that are recalled by the seller in accordance with the respective purchase agreement ("Recalls").

(2) Cumulative collections from inception through September 30, 2016, excluding collections on behalf of others.

(3) Cumulative Collections Multiple ("CCM") through September 30, 2016 refers to collections as a multiple of purchase price.



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## Total Estimated Collections to Purchase Price Multiple

The following table summarizes our purchases, resulting historical gross collections, and estimated remaining gross collections, by year of purchase (in thousands, except multiples):

|  | Purchase Price <sup>(1)</sup> | Historical Collections <sup>(2)</sup> | Estimated Remaining Collections <sup>(3)</sup> | Total Estimated Gross Collections | Total Estimated Gross Collections to Purchase Price |
|--|-------------------------------|---------------------------------------|--|-----------------------------------|---|
| Purchased consumer receivables:        |                               |                                       |  |                                   |   |
| United States:                         |                               |                                       |  |                                   |   |
| <2007                                  | \$ 719,081                    | \$ 2,206,341                          | \$ 12,831                                      | \$ 2,219,172                      | 3.1   |
| 2007                                   | 204,063                       | 523,056                               | 12,524   | 535,580                           | 2.6   |
| 2008                                   | 227,753                       | 618,557                               | 28,072   | 646,629                           | 2.8   |
| 2009                                   | 252,988                       | 784,958                               | 45,130   | 830,088                           | 3.3   |
| 2010                                   | 345,401                       | 1,005,458                             | 81,825   | 1,087,283                         | 3.1   |
| 2011                                   | 383,637                       | 976,352                               | 105,125  | 1,081,477                         | 2.8   |
| 2012                                   | 466,559                       | 973,926                               | 173,121  | 1,147,047                         | 2.5   |
| 2013 <sup>(4)</sup>                    | 512,897                       | 1,017,052                             | 387,739  | 1,404,791                         | 2.7   |
| 2014 <sup>(4)</sup>                    | 519,221                       | 625,341                               | 464,800  | 1,090,141                         | 2.1   |
| 2015                                   | 477,528                       | 283,533                               | 557,493  | 841,026                           | 1.8   |
| 2016                                   | 378,369                       | 62,695                                | 636,842  | 699,537                           | 1.8   |
| Subtotal                               | 4,487,497                     | 9,077,269                             | 2,505,502                                      | 11,582,771                        | 2.6   |
| Europe:                                |                               |                                       |  |                                   |   |
| 2013 <sup>(4)</sup>                    | 619,079                       | 725,776                               | 902,164  | 1,627,940                         | 2.6   |
| 2014 <sup>(4)</sup>                    | 630,343                       | 455,613                               | 835,493  | 1,291,106                         | 2.0   |
| 2015 <sup>(4)</sup>                    | 423,359                       | 162,797                               | 627,982  | 790,779                           | 1.9   |
| 2016                                   | 222,361                       | 27,077                                | 417,317  | 444,394                           | 2.0   |
| Subtotal                               | 1,895,142                     | 1,371,263                             | 2,782,956                                      | 4,154,219                         | 2.2   |
| Other geographies:                     |                               |                                       |  |                                   |   |
| 2012                                   | 6,706                         | 8,011                                 | 2,194  | 10,205                            | 1.5   |
| 2013                                   | 29,568                        | 38,106                                | 6,502  | 44,608                            | 1.5   |
| 2014                                   | 88,227                        | 39,480                                | 117,044  | 156,524                           | 1.8   |
| 2015                                   | 91,290                        | 59,350                                | 134,054  | 193,404                           | 2.1   |
| 2016                                   | 60,627                        | 19,243                                | 100,161  | 119,404                           | 2.0   |
| Subtotal                               | 276,418                       | 164,190                               | 359,955  | 524,145                           | 1.9   |
| Purchased U.S. bankruptcy receivables: |                               |                                       |  |                                   |   |
| 2010                                   | 11,971                        | 26,292                                | 6  | 26,298                            | 2.2   |
| 2011                                   | 1,642                         | 4,564                                 | 15   | 4,579                             | 2.8   |
| 2012                                   | 82,674                        | 90,662                                | 7,806  | 98,468                            | 1.2   |
| 2013                                   | 39,833                        | 70,879                                | 11,042   | 81,921                            | 2.1   |
| 2014                                   | —                             | —                                     | —  | —                                 | —   |
| 2015                                   | 24,372                        | 2,277                                 | 25,731   | 28,008                            | 1.1   |
| 2016                                   | 33,777                        | 370                                   | 39,531   | 39,901                            | 1.2   |
| Subtotal                               | 194,269                       | 195,044                               | 84,131   | 279,175                           | 1.4   |
| Total                                  | \$ 6,853,326                  | \$ 10,807,766                         | \$ 5,732,544                                   | \$ 16,540,310                     | 2.4   |

(1) Adjusted for Put-Backs and Recalls.

(2) Cumulative collections from inception through September 30, 2016, excluding collections on behalf of others.

(3) ERC for purchased consumer receivables includes \$77.9 million related to accounts that converted to bankruptcy after purchase.

(4) Includes portfolios acquired in connection with certain business combinations.

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## Estimated Remaining Gross Collections by Year of Purchase

The following table summarizes our estimated remaining gross collections by year of purchase (in thousands):

| Estimated Remaining Gross Collections by Year of Purchase <sup>(1), (2)</sup> |                     |             |             |           |           |           |           |           |           |           |             |
|---|---------------------|-------------|-------------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-------------|
|   | 2016 <sup>(3)</sup> | 2017        | 2018        | 2019      | 2020      | 2021      | 2022      | 2023      | 2024      | >2024     | Total       |
| Purchased consumer receivables:   |                     |             |             |           |           |           |           |           |           |           |             |
| United States:  |                     |             |             |           |           |           |           |           |           |           |             |
| <2007   | \$2,652             | \$5,782     | \$2,426     | \$1,317   | \$528     | \$126     | \$—       | \$—       | \$—       | \$—       | \$12,831    |
| 2007  | 1,978               | 4,459       | 2,664       | 1,628     | 992       | 602       | 201       | —         | —         | —         | 12,524      |
| 2008  | 3,594               | 10,507      | 5,864       | 3,449     | 2,147     | 1,332     | 845       | 334       | —         | —         | 28,072      |
| 2009  | 5,946               | 16,146      | 9,411       | 5,782     | 3,330     | 2,073     | 1,317     | 838       | 287       | —         | 45,130      |
| 2010  | 10,752              | 30,864      | 14,451      | 9,381     | 6,223     | 4,175     | 2,707     | 1,760     | 1,144     | 368       | 81,825      |
| 2011  | 12,795              | 40,525      | 20,068      | 12,197    | 7,767     | 5,180     | 3,236     | 1,729     | 974       | 654       | 105,125     |
| 2012  | 18,318              | 64,092      | 34,897      | 21,148    | 13,513    | 8,735     | 5,540     | 2,959     | 1,828     | 2,091     | 173,121     |
| 2013 <sup>(4)</sup>   | 34,632              | 119,312     | 80,431      | 53,791    | 36,135    | 24,092    | 15,757    | 9,915     | 5,657     | 8,017     | 387,739     |
| 2014 <sup>(4)</sup>   | 39,404              | 141,870     | 104,273     | 61,117    | 40,081    | 25,539    | 18,238    | 12,953    | 8,911     | 12,414    | 464,800     |
| 2015  | 46,105              | 162,943     | 128,002     | 83,049    | 53,090    | 30,778    | 19,875    | 14,133    | 9,917     | 9,601     | 557,493     |
| 2016  | 29,700              | 177,178     | 166,565     | 101,328   | 63,113    | 38,315    | 22,907    | 15,665    | 11,389    | 10,682    | 636,842     |
| Subtotal  | 205,876             | 773,678     | 569,052     | 354,187   | 226,919   | 140,947   | 90,623    | 60,286    | 40,107    | 43,827    | 2,505,500   |
| Europe:   |                     |             |             |           |           |           |           |           |           |           |             |
| 2013 <sup>(4)</sup>   | 30,879              | 119,651     | 123,359     | 105,795   | 90,925    | 79,266    | 70,631    | 63,492    | 57,172    | 160,994   | 902,164     |
| 2014 <sup>(4)</sup>   | 29,263              | 111,087     | 113,097     | 97,424    | 83,787    | 72,270    | 63,562    | 56,675    | 50,104    | 158,224   | 835,493     |
| 2015 <sup>(4)</sup>   | 21,592              | 82,694      | 83,011      | 69,897    | 58,305    | 50,760    | 44,808    | 40,186    | 35,929    | 140,800   | 627,982     |
| 2016  | 11,015              | 50,974      | 59,281      | 51,272    | 42,070    | 34,741    | 28,196    | 24,446    | 21,918    | 93,404    | 417,317     |
| Subtotal  | 92,749              | 364,406     | 378,748     | 324,388   | 275,087   | 237,037   | 207,197   | 184,799   | 165,123   | 553,422   | 2,782,955   |
| Other geographies:  |                     |             |             |           |           |           |           |           |           |           |             |
| 2012  | 183                 | 655         | 489         | 317       | 234       | 197       | 119       | —         | —         | —         | 2,194       |
| 2013  | 761                 | 2,445       | 1,741       | 808       | 445       | 193       | 96        | 13        | —         | —         | 6,502       |
| 2014  | 3,452               | 13,938      | 43,367      | 37,571    | 12,446    | 2,048     | 1,458     | 1,444     | 1,320     | —         | 117,044     |
| 2015  | 8,428               | 31,683      | 30,889      | 22,518    | 16,381    | 10,019    | 6,423     | 3,497     | 2,242     | 1,974     | 134,054     |
| 2016  | 5,568               | 21,194      | 23,595      | 18,120    | 13,407    | 8,621     | 3,882     | 2,354     | 1,704     | 1,716     | 100,161     |
| Subtotal  | 18,392              | 69,915      | 100,081     | 79,334    | 42,913    | 21,078    | 11,978    | 7,308     | 5,266     | 3,690     | 359,955     |
| Purchased U.S. bankruptcy receivables:  |                     |             |             |           |           |           |           |           |           |           |             |
| 2010  | 6                   | —           | —           | —         | —         | —         | —         | —         | —         | —         | 6           |
| 2011  | 13                  | 2           | —           | —         | —         | —         | —         | —         | —         | —         | 15          |
| 2012  | 1,701               | 4,634       | 1,471       | —         | —         | —         | —         | —         | —         | —         | 7,806       |
| 2013  | 2,463               | 6,945       | 1,598       | 36        | —         | —         | —         | —         | —         | —         | 11,042      |
| 2014  | —                   | —           | —           | —         | —         | —         | —         | —         | —         | —         | —           |
| 2015  | 795                 | 5,138       | 7,244       | 6,916     | 4,512     | 697       | 183       | 120       | 81        | 45        | 25,731      |
| 2016  | 180                 | 4,520       | 9,343       | 10,235    | 9,167     | 4,900     | 595       | 264       | 173       | 154       | 39,531      |
| Subtotal  | 5,158               | 21,239      | 19,656      | 17,187    | 13,679    | 5,597     | 778       | 384       | 254       | 199       | 84,131      |
| Total   | \$322,175           | \$1,229,238 | \$1,067,537 | \$775,096 | \$558,598 | \$404,659 | \$310,576 | \$252,777 | \$210,750 | \$601,138 | \$5,732,000 |

ERC for Zero Basis Portfolios can extend beyond our collection forecasts. As of September 30, 2016, ERC for Zero Basis Portfolios include approximately \$172.0 million for purchased consumer receivables in the United States. ERC for Zero Basis Portfolios for purchased consumer receivables in Europe and other geographies and purchased U.S. bankruptcy receivables were immaterial.

(2)ERC for purchased consumer receivables includes \$77.9 million related to accounts that converted to bankruptcy after purchase. The collection forecast of each pool is generally estimated up to 120 months in the United States

and up to 180 months in Europe. Expected collections beyond the 120 month collection forecast in the United States are included in ERC but are not included in the calculation of IRRs.

(3) 2016 amount consists of three months data from October 1, 2016 to December 31, 2016.

(4) Includes portfolios acquired in connection with certain business combinations.



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## Unamortized Balances of Portfolios

The following table summarizes the remaining unamortized balances of our purchased receivable portfolios by year of purchase (in thousands, except percentages):

|  | Unamortized<br>Balance as of<br>September 30,<br>2016 | Purchase<br>Price <sup>(1)</sup> | Unamortized<br>Balance as a<br>Percentage of<br>Purchase Price | Unamortized<br>Balance as a<br>Percentage<br>of Total |       |   |
|--|---|----------------------------------|--|---|-------|---|
| Purchased consumer receivables:        |   |                                  |  |   |       |   |
| United States:                         |   |                                  |  |   |       |   |
| 2007                                   | \$ 942  | \$204,063                        | 0.5  | %   | 0.1   | % |
| 2008                                   | 3,631   | 227,753                          | 1.6  | %   | 0.4   | % |
| 2009                                   | —   | 252,988                          | 0.0  | %   | 0.0   | % |
| 2010                                   | 1,902   | 345,401                          | 0.6  | %   | 0.2   | % |
| 2011                                   | 9,237   | 383,637                          | 2.4  | %   | 0.9   | % |
| 2012                                   | 39,101  | 466,559                          | 8.4  | %   | 3.8   | % |
| 2013 <sup>(2)</sup>                    | 102,270   | 512,897                          | 19.9   | %   | 9.9   | % |
| 2014 <sup>(2)</sup>                    | 205,503   | 519,221                          | 39.6   | %   | 19.9  | % |
| 2015                                   | 318,022   | 477,528                          | 66.6   | %   | 30.8  | % |
| 2016                                   | 350,650   | 378,369                          | 92.7   | %   | 34.0  | % |
| Subtotal                               | 1,031,258   | 3,768,416                        | 27.4   | %   | 100.0 | % |
| Europe:                                |   |                                  |  |   |       |   |
| 2013 <sup>(2)</sup>                    | 286,472   | 619,079                          | 46.3   | %   | 25.4  | % |
| 2014 <sup>(2)</sup>                    | 341,855   | 630,343                          | 54.2   | %   | 30.4  | % |
| 2015 <sup>(2)</sup>                    | 289,982   | 423,359                          | 68.5   | %   | 25.8  | % |
| 2016                                   | 206,978   | 222,361                          | 93.1   | %   | 18.4  | % |
| Subtotal                               | 1,125,287   | 1,895,142                        | 59.4   | %   | 100.0 | % |
| Other geographies:                     |   |                                  |  |   |       |   |
| 2013                                   | 1,408   | 29,568                           | 4.8  | %   | 0.8   | % |
| 2014                                   | 61,055  | 88,227                           | 69.2   | %   | 34.5  | % |
| 2015                                   | 61,125  | 91,290                           | 67.0   | %   | 34.5  | % |
| 2016                                   | 53,454  | 60,627                           | 88.2   | %   | 30.2  | % |
| Subtotal                               | 177,042   | 269,712                          | 65.6   | %   | 100.0 | % |
| Purchased U.S. bankruptcy receivables: |   |                                  |  |   |       |   |
| 2012                                   | 7,187   | 82,674                           | 8.7  | %   | 11.1  | % |
| 2013                                   | —   | 39,833                           | 0.0  | %   | 0.0   | % |
| 2014                                   | —   | —                                | —  |   | —     |   |
| 2015                                   | 23,104  | 24,372                           | 94.8   | %   | 36.0  | % |
| 2016                                   | 33,953  | 33,777                           | 100.5  | %   | 52.9  | % |
| Subtotal                               | 64,244  | 180,656                          | 35.6   | %   | 100.0 | % |
| Total                                  | \$ 2,397,831  | \$6,113,926                      | 39.2   | %   | 100.0 | % |

(1) Purchase price refers to the cash paid to a seller to acquire a portfolio less Put-Backs, Recalls, and other adjustments.

(2) Includes portfolios acquired in connection with certain business combinations.

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## Estimated Future Amortization of Portfolios

As of September 30, 2016, we had \$2.4 billion in investment in receivable portfolios. This balance will be amortized based upon current projections of cash collections in excess of revenue applied to the principal balance. The estimated amortization of the investment in receivable portfolios balance is as follows (in thousands):

| Years Ending December 31, | Purchased<br>Consumer<br>Receivables<br>United States | Purchased<br>Consumer<br>Receivables<br>Europe | Purchased<br>Consumer<br>Receivables<br>Other<br>Geographies | Purchased<br>U.S.<br>Bankruptcy<br>Receivables | Total<br>Amortization |
|---------------------------|---|--|--|--|-----------------------|
| 2016 <sup>(1)</sup>       | \$ 50,679   | \$ 22,923                                      | \$ 3,004   | \$ 1,770                                       | \$ 78,376             |
| 2017                      | 280,995   | 98,003   | 11,125   | 11,121   | 401,244               |
| 2018                      | 262,744   | 143,417  | 51,893   | 15,787   | 473,841               |
| 2019                      | 160,234   | 121,454  | 50,332   | 15,690   | 347,710               |
| 2020                      | 104,287   | 99,685   | 28,081   | 12,962   | 245,015               |
| 2021                      | 65,103  | 84,234   | 12,811   | 5,398  | 167,546               |
| 2022                      | 43,609  | 75,068   | 10,178   | 720  | 129,575               |
| 2023                      | 31,143  | 71,521   | 3,928  | 403  | 106,995               |
| 2024                      | 20,153  | 81,898   | 2,601  | 393  | 105,045               |
| 2025                      | 9,897   | 65,487   | 2,013  | —  | 77,397                |
| 2026                      | 2,414   | 67,618   | 1,076  | —  | 71,108                |
| 2027                      | —   | 70,151   | —  | —  | 70,151                |
| 2028                      | —   | 70,232   | —  | —  | 70,232                |
| 2029                      | —   | 33,025   | —  | —  | 33,025                |
| 2030                      | —   | 16,855   | —  | —  | 16,855                |
| 2031                      | —   | 3,716  | —  | —  | 3,716                 |
| Total                     | \$ 1,031,258  | \$ 1,125,287                                   | \$ 177,042   | \$ 64,244                                      | \$ 2,397,831          |

(1) 2016 amount consists of three months data from October 1, 2016 to December 31, 2016.

## Headcount by Function by Geographic Location

The following table summarizes our headcount by function by geographic location:

|                          | Headcount as of September 30, |               |       |               |
|--------------------------|-------------------------------|---------------|-------|---------------|
|                          | 2016                          |               | 2015  |               |
|                          | Domes                         | International | Domes | International |
| General & Administrative | 915                           | 2,152         | 924   | 1,795         |
| Account Manager          | 266                           | 3,229         | 274   | 2,644         |
| Total                    | 1,181                         | 5,381         | 1,198 | 4,439         |

(1) Headcount as of September 30, 2015 includes 80 Propel employees.

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## Purchases by Quarter

The following table summarizes the consumer receivable portfolios and bankruptcy receivables we purchased by quarter, and the respective purchase prices (in thousands):

| Quarter                | # of Accounts | Face Value  | Purchase Price |
|------------------------|---------------|-------------|----------------|
| Q1 2014 <sup>(1)</sup> | 1,104         | \$4,288,159 | \$467,565      |
| Q2 2014                | 1,210         | 3,075,343   | 225,762        |
| Q3 2014 <sup>(1)</sup> | 2,203         | 3,970,145   | 299,509        |
| Q4 2014                | 859           | 2,422,128   | 258,524        |
| Q1 2015                | 734           | 1,041,011   | 125,154        |
| Q2 2015 <sup>(1)</sup> | 2,970         | 5,544,885   | 418,780        |
| Q3 2015                | 1,267         | 2,085,381   | 187,180        |
| Q4 2015 <sup>(1)</sup> | 2,363         | 4,068,252   | 292,608        |
| Q1 2016                | 1,450         | 3,544,338   | 256,753        |
| Q2 2016                | 946           | 2,841,527   | 233,116        |
| Q3 2016                | 874           | 1,475,381   | 206,359        |

(1) Includes portfolios acquired in connection with certain business combinations.

## Liquidity and Capital Resources

## Liquidity

The following table summarizes our cash flow activity, including the cash flows from discontinued operations, for the periods presented (in thousands):

Nine Months  
Ended  
September 30,  
2016      2015

(Unaudited)

|   |          |           |
|---|----------|-----------|
| Net cash provided by operating activities | \$85,268 | \$63,381  |
| Net cash used in investing activities     | (91,613) | (354,905) |
| Net cash provided by financing activities | 13,687   | 345,855   |

## Operating Cash Flows

Cash flows from operating activities represent the cash receipts and disbursements related to all of our activities other than investing and financing activities. Operating cash flow is derived by adjusting net income for non-cash operating items such as depreciation and amortization, allowance charges and stock-based compensation charges, and changes in operating assets and liabilities which reflect timing differences between the receipt and payment of cash associated with transactions and when they are recognized in results of operations.

Net cash provided by operating activities was \$85.3 million and \$63.4 million during the nine months ended September 30, 2016 and 2015, respectively. Cash provided by operating activities during the nine months ended September 30, 2016 was primarily related to net income of \$5.5 million, adjustments for discontinued operations, various non-cash add backs in operating activities, including portfolio allowance charges, and changes in operating assets and liabilities. Cash provided by operating activities during the nine months ended September 30, 2015 was primarily related to net income of \$45.8 million, adjustments for discontinued operations, various non-cash add backs in operating activities, and changes in operating assets and liabilities.

## Investing Cash Flows

Net cash used in investing activities was \$91.6 million and \$354.9 million during the nine months ended September 30, 2016 and 2015, respectively.

The cash flows used in investing activities during the nine months ended September 30, 2016 were primarily related to receivable portfolio purchases of \$712.7 million, offset by collection proceeds applied to the principal of our

receivable portfolios in the amount of \$507.6 million and \$106.0 million of proceeds from divestiture of Propel, net of cash divested. The

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cash flows used in investing activities during the nine months ended September 30, 2015 were primarily related to cash paid for the dlc Acquisition, net of cash acquired, of \$236.2 million, receivable portfolio purchases (excluding the portfolios acquired from the dlc Acquisition of \$216.0 million) of \$550.0 million, offset by collection proceeds applied to the principal of our receivable portfolios in the amount of \$488.2 million.

Capital expenditures for fixed assets acquired with internal cash flows were \$16.5 million and \$15.8 million for nine months ended September 30, 2016 and 2015, respectively.

### Financing Cash Flows

Net cash provided by financing activities was \$13.7 million during the nine months ended September 30, 2016. Net cash provided by financing activities was \$345.9 million during the nine months ended September 30, 2015. Net cash used in financing activities from discontinued operations was \$15.5 million during the nine months ended September 30, 2016. Net cash provided by discontinued operations was \$37.0 million during the nine months ended September 30, 2015.

The cash provided by financing activities during the nine months ended September 30, 2016 primarily reflects \$455.8 million in borrowings under our credit facilities, offset by \$444.0 million in repayments of amounts outstanding under our credit facilities. The cash provided by financing activities during the nine months ended September 30, 2015 primarily reflects \$911.6 million in borrowings under our credit facilities, offset by \$471.6 million in repayments of amounts outstanding under our credit facilities and \$33.2 million in repurchases of our common stock.

### Capital Resources

Historically, we have met our cash requirements by utilizing our cash flows from operations, bank borrowings, convertible debt offerings, and equity offerings. From time to time, depending on the capital markets, we consider additional financings to fund our operations and acquisitions. Our primary cash requirements have included the purchase of receivable portfolios, the acquisition of U.S. and international entities, operating expenses, the payment of interest and principal on borrowings, and the payment of income taxes.

On March 24, 2016, we amended our revolving credit facility and term loan facility pursuant to Amendment No. 3 to the Second Amended and Restated Credit Agreement (as amended, the “Restated Credit Agreement”). The Restated Credit Agreement includes a revolving credit facility of \$742.6 million (the “Revolving Credit Facility”), a term loan facility of \$158.8 million (the “Term Loan Facility”, and together with the Revolving Credit Facility, the “Senior Secured Credit Facilities”), and an accordion feature that allows us to increase the Revolving Credit Facility by an additional \$250.0 million (\$55.0 million of which was exercised in November 2015). The Senior Secured Credit Facilities have a five-year maturity, expiring in February 2019, except with respect to two subtranches of the Term Loan Facility of \$60.0 million and \$6.3 million, expiring in February 2017 and November 2017, respectively. As of September 30, 2016, we had \$701.0 million outstanding and \$175.6 million of availability under the Senior Secured Credit Facilities, excluding the \$195.0 million available under the accordion.

On October 6, 2016, Cabot Financial (Luxembourg) S.A. (“Cabot Financial”), an indirect subsidiary of Encore, issued £350 million (approximately \$442.6 million) in aggregate principal amount of 7.50% Senior Secured Notes due 2023 (the “Cabot 2023 Notes”). The majority of the proceeds from the offering were used to redeem in full the £265.0 million, 10.375% Cabot 2019 Senior Secured Notes and partially repay amounts outstanding under the Cabot Credit Facility.

Through Cabot Financial (UK) Limited (“Cabot Financial UK”), an indirect subsidiary, we have a revolving credit facility (the “Cabot Credit Facility”), the Cabot Credit Facility was amended on October 6, 2016 that increased the total commitment amount from £200.0 million to £250.0 million. The Cabot Credit Facility includes an uncommitted accordion facility that will allow the facility to be increased by an additional £50.0 million, subject to obtaining the requisite commitments and compliance with the terms of Cabot Financial UK’s other indebtedness. As of September 30, 2016, we had £88.0 million (approximately \$114.3 million) outstanding and £112.0 million (approximately \$145.5 million) of availability under the Cabot Credit Facility.

Currently, all of our portfolio purchases are funded with cash from operations and borrowings under our Senior Secured Credit Facilities and our Cabot Credit Facility.

We are in compliance with all covenants under our financing arrangements. See Note 10, “Debt” to our condensed consolidated financial statements for a further discussion of our debt.

Our cash and cash equivalents at September 30, 2016 consisted of \$35.5 million held by U.S.-based entities and \$122.1 million held by foreign entities. Most of our cash and cash equivalents held by foreign entities is indefinitely reinvested and

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may be subject to material tax effects if repatriated. However, we believe that our U.S. sources of cash and liquidity are sufficient to meet our business needs in the United States and do not expect that we will need to repatriate the funds.

We believe that we have sufficient liquidity to fund our operations for at least the next twelve months, given our expectation of continued positive cash flows from operations, our cash and cash equivalents, our access to capital markets, and availability under our credit facilities. Our future cash needs will depend on our acquisitions of portfolios and businesses. The divestiture of Propel provided liquidity to deleverage our company and paid down our debt. Additionally, it is expected to improve our overall corporate return on invested capital and provide us additional liquidity for increased investment capital flexibility.

### Item 3 – Quantitative and Qualitative Disclosures About Market Risk

**Foreign Currency Exchange Rates.** We have operations in foreign countries, which expose us to foreign currency exchange rate fluctuations due to transactions denominated in foreign currencies. Our primary risk of loss due to foreign currency exchange rate risk is related to Euro to British Pound and Indian rupee to U.S. dollar exchange rates. We continuously evaluate and manage our foreign currency risk through the use of derivative financial instruments, including foreign currency forward contracts with financial counterparties where practicable. Such derivative instruments are viewed as risk management tools and are not used for speculative or trading purposes.

Beginning in 2016, we have currency exchange forward contracts to reduce the effects of currency exchange rate fluctuations between the British Pound and Euro. These derivative contracts generally mature within one to three months and are not designated as hedge instruments for accounting purposes. The gains or losses on these derivative contracts are recognized in other income or expense based on the changes in fair value.

As of September 30, 2016, we had outstanding foreign currency forward contracts that hedge our risk of foreign currency exchange between the British Pound and Euro with a fair value asset position of approximately \$0.8 million. The functional currency of the subsidiary that carries the hedge contracts is British Pound and the reporting currency is the U.S. dollar. We considered the historical trends in currency exchange rates and determined that it was reasonably possible that changes in exchange rates of 10% between the British Pound and the Euro and 10% between the British Pound and U.S. dollar could be experienced in the near term. If the Euro weakened by 10% against the British Pound and the U.S. dollar weakened by 10% against the British Pound as of September 30, 2016, the result would have an unfavorable effect to the fair value of the derivatives by approximately \$17.5 million. If the Euro strengthened by 10% against the British Pound and the U.S. dollar strengthened by 10% against the British Pound as of September 30, 2016, the result would have a favorable effect to the fair value of the derivatives by approximately \$15.8 million.

In addition, we have currency exchange forward contracts that hedge the forecasted monthly cash settlements resulting from the expenses incurred by our operations in India. These foreign currency forward contracts are designated as cash flow hedging instruments and qualify for hedge accounting treatment. Gains and losses arising from the effective portion of such contracts are recorded as a component of accumulated other comprehensive income (“OCI”) as gains and losses on derivative instruments, net of income taxes. The hedging gains and losses in OCI are subsequently reclassified into earnings in the same period in which the underlying transactions affect the Company’s earnings. If all or a portion of the forecasted transaction is cancelled, this would render all or a portion of the cash flow hedge ineffective and the Company would reclassify the ineffective portion of the hedge into earnings. The Company generally does not experience ineffectiveness of the hedge relationship and the accompanying consolidated financial statements do not include any such gains or losses.

As of September 30, 2016, our outstanding foreign currency forward contracts that hedge our risk of foreign currency exchange against the Indian rupee had a fair value asset position of \$0.6 million. We considered the historical trends in currency exchange rates and determined that it was reasonably possible that changes in exchange rates of 10% for the Indian rupee could be experienced in the near term. If the U.S. dollar weakened by 10% at September 30, 2016 this would have a negative impact to the fair value of the hedge of approximately \$2.6 million. If the U.S. dollar strengthened by 10% at September 30, 2016 this would have a positive impact to the fair value of the hedge of approximately \$4.6 million.

Interest Rates. At September 30, 2016, there had not been a material change in the interest rate risk information disclosed in Item 7A, "Quantitative and Qualitative Disclosures About Market Risk," of our Annual Report on Form 10-K for the fiscal year ended December 31, 2015.



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Item 4 – Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our periodic reports filed or submitted under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission (the “SEC”) and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, our management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives and accordingly, management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Based on their most recent evaluation, as of the end of the period covered by this Quarterly Report on Form 10-Q, our Chief Executive Officer and Chief Financial Officer have concluded our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act are effective.

Changes in Internal Control over Financial Reporting

No changes in our internal control over financial reporting occurred during the quarter ended September 30, 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II – OTHER INFORMATION

Item 1 – Legal Proceedings

Information with respect to this item may be found in Note 13, “Commitments and Contingencies,” to the condensed consolidated financial statements.

Item 1A – Risk Factors

There is no material change in the information reported under “Part I-Item 1A-Risk Factors” contained in our Annual Report on Form 10-K for the fiscal year ended December 31, 2015 and “Part II, Item 1A-Risk Factors” in our Quarterly Report on Form 10-Q for the quarter ended June 30, 2016.

Item 6 – Exhibits

- 3.1 Restated Certificate of Incorporation (incorporated by reference to Exhibit 3.1 to Amendment No. 2 to the Company’s Registration Statement on Form S-1/A filed on June 14, 1999, File No. 333-77483)
  - 3.2 Certificate of Amendment to the Certificate of Incorporation (incorporated by reference to Exhibit 3.1 to the Company’s Current Report on Form 8-K filed on April 4, 2002)
  - 3.3 Bylaws, as amended through February 8, 2011 (incorporated by reference to Exhibit 3.3 to the Company’s Annual Report on Form 10-K filed on February 14, 2011)
  - 10.1+ First Amendment to Non-Employee Director Deferred Stock Compensation Plan (filed herewith)
  - 31.1 Certification of the Principal Executive Officer pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith)
  - 31.2 Certification of the Principal Financial Officer pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith)
  - 32.1 Certifications of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith)
  - 101.INS XBRL Instance Document (filed herewith)
  - 101.SCH XBRL Taxonomy Extension Schema Document (filed herewith)
  - 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document (filed herewith)
  - 101.DEF XBRL Taxonomy Extension Definition Linkbase Document (filed herewith)
  - 101.LAB XBRL Taxonomy Extension Label Linkbase Document (filed herewith)
  - 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document (filed herewith)
- +Management contract or compensation plan or arrangement.

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SIGNATURES

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

ENCORE CAPITAL GROUP, INC.

By: /s/ Jonathan C. Clark  
Jonathan C. Clark  
Executive Vice President,  
Chief Financial Officer and Treasurer

Date: November 9, 2016