ENCORE CAPITAL GROUP INC
Form 10-Q
August 02, 2010
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended June 30, 2010

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 **(State or other jurisdiction of** **incorporation or organization)**	**48-1090909** **(IRS Employer** **Identification No.)**
8875 Aero Drive, Suite 200 **San Diego, California** **(Address of principal executive offices)**	**92123** **(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)

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 x 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 x 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 x

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

Class	Outstanding at July 27, 2010
Common Stock, $0.01 par value	23,805,717 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)

	June 30, 2010	December 31, 2009
Assets		
Cash and cash equivalents	$ 10,402	$ 8,388
Accounts receivable, net	2,478	3,134
Investment in receivable portfolios, net	566,815	526,877
Deferred court costs	25,954	25,957
Property and equipment, net	11,234	9,427
Prepaid income tax	2,039	
Other assets	9,793	4,252
Goodwill	15,985	15,985
Identifiable intangible assets, net	943	1,139
Total assets	$ 645,643	$ 595,159
Liabilities and stockholders equity		
Liabilities:		
Accounts payable and accrued liabilities	$ 22,028	$ 21,815
Income taxes payable		2,681
Deferred tax liabilities, net	16,958	16,980
Deferred revenue	4,808	5,481
Debt	328,656	303,075
Other liabilities	1,066	2,036
Total liabilities	373,516	352,068
Commitments and contingencies and subsequent events		
Stockholders 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, 23,785 shares and 23,359 shares issued and outstanding as of June 30, 2010 and December 31, 2009, respectively	238	234
Additional paid-in capital	110,117	104,261
Accumulated earnings	162,433	139,842
Accumulated other comprehensive loss	(661)	(1,246)
Total stockholders equity	272,127	243,091
Total liabilities and stockholders equity	$ 645,643	$ 595,159

See accompanying notes to condensed consolidated financial statements

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ENCORE CAPITAL GROUP, INC.

Condensed Consolidated Statements of Income

(In Thousands, Except Per Share Amounts)

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	**2009**	**2010**	**2009**
Revenue				
Revenue from receivable portfolios, net	$ 91,845	$ 73,965	$ 174,752	$ 146,240
Servicing fees and other related revenue	4,386	4,070	8,817	8,241
Total revenue	96,231	78,035	183,569	154,481
Operating expenses				
Salaries and employee benefits (excluding stock-based compensation expense)	16,484	14,762	31,969	28,719
Stock-based compensation expense	1,446	994	3,207	2,074
Cost of legal collections	31,235	28,626	57,668	58,573
Other operating expenses	9,027	6,598	18,141	12,578
Collection agency commissions	6,413	4,797	11,709	7,688
General and administrative expenses	7,425	7,097	14,304	12,794
Depreciation and amortization	752	620	1,425	1,243
Total operating expenses	72,782	63,494	138,423	123,669
Income before other (expense) income and income taxes	23,449	14,541	45,146	30,812
Other (expense) income				
Interest expense	(4,880)	(3,958)	(9,418)	(8,231)
Gain on repurchase of convertible notes, net		215		3,268
Other (expense) income	(90)	9	102	(72)
Total other expense	(4,970)	(3,734)	(9,316)	(5,035)
Income before income taxes	18,479	10,807	35,830	25,777
Provision for income taxes	(6,749)	(4,166)	(13,239)	(10,139)
Net income	$ 11,730	$ 6,641	$ 22,591	$ 15,638
Weighted average shares outstanding:				
Basic	23,713	23,168	23,673	23,145
Diluted	24,958	23,971	24,897	23,811
Earnings per share:				
Basic	$ 0.49	$ 0.29	$ 0.95	$ 0.68
Diluted	$ 0.47	$ 0.28	$ 0.91	$ 0.66

See accompanying notes to condensed consolidated financial statements

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ENCORE CAPITAL GROUP, INC.

Condensed Consolidated Statements of Stockholders Equity and Comprehensive Income

(Unaudited, In Thousands)

	Common Stock		Additional		Accumulated Other		
	Shares	Par	Paid-In Capital	Accumulated Earnings	Comprehensive Income (loss)	Total Equity	Comprehensive Income
Balance at December 31, 2009	23,359	$ 234	$ 104,261	$ 139,842	$ (1,246)	$ 243,091	$
Net income				22,591		22,591	22,591
Other comprehensive gain:							
Unrealized gain on cash flow hedge, net of tax					585	585	585
Exercise of stock options and issuance of share-based awards, net of shares withheld for employee taxes	426	4	432			436	
Stock-based compensation			3,207			3,207	
Settlement of call options and warrants associated with convertible notes, net			524			524	
Tax benefit related to stock-based compensation			1,693			1,693	
Balance at June 30, 2010	23,785	$ 238	$ 110,117	$ 162,433	$ (661)	$ 272,127	$ 23,176

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)

	Six Months Ended June 30,	
	2010	**2009**
Operating activities:		
Net income	$ 22,591	$ 15,638
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,425	1,243
Amortization of loan costs and debt discount	2,194	2,160
Stock-based compensation expense	3,207	2,074
Gain on repurchase of convertible notes, net		(3,268)
Deferred income tax expense	(22)	360
Excess tax benefit from stock-based payment arrangements	(1,813)	(28)
Provision for allowances on receivable portfolios, net	10,720	9,991
Changes in operating assets and liabilities		
Other assets	39	(2,456)
Deferred court costs	3	(1,425)
Prepaid income tax and income taxes payable	(3,027)	8,577
Deferred revenue	(673)	197
Accounts payable, accrued liabilities and other liabilities	(1,072)	611
Net cash provided by operating activities	33,572	33,674
Investing activities:		
Purchases of receivable portfolios	(164,968)	(137,946)
Collections applied to investment in receivable portfolios, net	112,446	81,163
Proceeds from put-backs of receivable portfolios	1,864	1,430
Purchases of property and equipment	(1,647)	(1,400)
Net cash used in investing activities	(52,305)	(56,753)
Financing activities:		
Payment of loan costs	(4,660)	
Proceeds from revolving credit facility	53,000	62,500
Repayment of revolving credit facility	(31,000)	(21,500)
Repurchase of convertible notes		(22,262)
Proceeds from net settlement of certain call options	524	
Proceeds from exercise of stock options	1,688	29
Excess tax benefit from stock-based payment arrangements	1,813	28
Repayment of capital lease obligations	(618)	(122)
Net cash provided by financing activities	20,747	18,673
Net increase (decrease) in cash and cash equivalents	2,014	(4,406)
Cash and cash equivalents, beginning of period	8,388	10,341
Cash and cash equivalents, end of period	$ 10,402	$ 5,935

Supplemental disclosures of cash flow information:				
Cash paid for interest	$	6,994	$	6,435
Cash paid for income taxes	$	16,544	$	1,626
Supplemental schedule of non-cash investing and financing activities:				
Fixed assets acquired through capital lease	$	1,389	$	

See accompanying notes to condensed consolidated financial statements

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, the Company), is a systems-driven purchaser and manager of charged-off consumer receivable portfolios and, through its wholly owned subsidiary Ascension Capital Group, Inc. (Ascension), a provider of bankruptcy services to the finance industry. The Company purchases portfolios of defaulted consumer receivables and manages them by partnering 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, auto finance companies and telecommunication companies which the Company purchases at deep discounts. The Company s success hinges on it understanding, measuring, and predicting the distressed consumer s behavior. The Company has invested heavily to build one of the industry s strongest analytic platforms. The Company purchases receivables based on account-level valuation methods, and employs a suite of proprietary statistical models across the full extent of its operations. Moreover, the Company has one of the industry s largest distressed consumer databases, comprised of approximately 20 million consumer accounts. As a result, the Company has been able to historically realize significant returns from the receivables it acquires. The Company s performance derives from its sophisticated and widespread use of analytics, its investments in data and consumer intelligence, its cost leadership position (based on the Company s enterprise-wide, account-level cost database as well as its India facility), and its commitment to see principled intent drive every consumer interaction. The Company maintains strong relationships with many of the largest credit providers in the United States, and possesses one of the industry s best collection staff retention rates.

In addition, the Company provides bankruptcy support services to some of the largest companies in the financial services industry through its Ascension subsidiary. Leveraging a proprietary software platform dedicated to bankruptcy servicing, Ascension s operational platform integrates lenders, trustees, and consumers across the bankruptcy lifecycle.

Acquisitions of receivable portfolios are financed by operations and by borrowings from third parties. See Note 9 for further discussion of the Company s debt.

Financial Statement Preparation

The accompanying interim condensed consolidated financial statements have been prepared by Encore, without audit, in accordance with the instructions to Form 10-Q, and Rule 10-01 of Regulation S-X promulgated by the Securities and Exchange Commission 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.

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 results of operations, financial position 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, 2009. 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 accounting principles generally accepted in the United States 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.

Principles of Consolidation

The Company s condensed consolidated financial statements include the assets, liabilities and operating results of its wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated.

New Accounting Pronouncements

In October 2009, the Financial Accounting Standards Board issued Accounting Standards Update No. 2009-13, *Revenue Recognition (Topic 605): Multiple-Deliverable Revenue Arrangements a consensus of the FASB Emerging Issues Task Force*, which establishes a selling price hierarchy for determining the selling price of a deliverable, and eliminates the residual method of allocation. This update requires the arrangement consideration be allocated at the inception of the arrangement to all deliverables using the relative selling price method. This update is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. The Company is currently analyzing the impact of this update, if any, to its consolidated financial statements.

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Note 2: Earnings per Share

Basic earnings per share is calculated by dividing net earnings available to common stockholders 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 and restricted stock units.

The components of basic and diluted earnings per share are as follows *(in thousands, except earnings per share)*:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
Net income available for common shareholders	$ 11,730	$ 6,641	$ 22,591	$ 15,638
Weighted average outstanding shares of common stock	23,713	23,168	23,673	23,145
Dilutive effect of stock-based awards	1,245	803	1,224	666
Common stock and common stock equivalents	24,958	23,971	24,897	23,811
Earnings per share:				
Basic[(1)]	$ 0.49	$ 0.29	$ 0.95	$ 0.68
Diluted[(2)]	$ 0.47	$ 0.28	$ 0.91	$ 0.66

(1) Represents net income available for common shareholders divided by weighted average outstanding shares of common stock.

(2) Represents net income available for common shareholders divided by common stock and common stock equivalents.

Employee stock options to purchase approximately 259,000 and 264,000 shares of common stock during the three and six months ended June 30, 2010, respectively, and employee stock options to purchase approximately 1,346,000 shares of common stock during the three and six months ended June 30, 2009, were outstanding but not included in the computation of diluted earnings per share because the effect on diluted earnings per share would be anti-dilutive.

Note 3: 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 that reflect the reporting entity s own assumptions.

Liabilities measured at fair value on a recurring basis at June 30, 2010 are summarized below (*in thousands*):

	Level 1	Level 2	Level 3	Total
Liabilities				
Foreign exchange contracts	$	$ 120	$	$ 120
Interest rate swap agreements	$	$ 946	$	$ 946

Fair values of derivative instruments included in Level 2 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 exchange rates, and forward and spot prices for currencies. As of June 30, 2010, the Company did not have any financial instruments carried at fair value that required Level 3 measurement.

Financial instruments not required to be carried at fair value

Borrowings under the Company s revolving credit facility are carried at historical cost, adjusted for additional borrowings less principal repayments, which approximates fair value. The Company s Convertible Notes are carried at historical cost, adjusted for repurchases and debt discount. The fair value estimate for these notes incorporates quoted market prices at the balance sheet date, which was determined to be approximately equal to book value as of June 30, 2010 and December 31, 2009. For investment in receivable portfolios, there is no active market or observable inputs for the fair value estimation. The Company considers it not practical to attempt to estimate the fair value of such financial instruments due to the excessive costs that would be incurred in doing so.

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Note 4: Derivatives and Hedging Instruments

The Company uses derivative instruments to manage risks related to interest rates and foreign currency. The Company s outstanding interest rate swap contracts and foreign exchange contracts qualify for hedge accounting treatment under the authoritative guidance for derivatives and hedging.

Interest Rate Swaps

The Company may periodically enter into derivative financial instruments, typically interest rate swap agreements, to reduce its exposure to fluctuations in interest rates on variable interest rate debt and their impact on earnings and cash flows. As of June 30, 2010, the Company has one interest rate swap agreement outstanding with a notional amount of $25.0 million and an expiration date of April 2011. Under the swap agreement, the Company receives floating interest rate payments and makes interest payments based on a fixed interest rate of 5.01%. The Company intends to continue electing the one-month reserve-adjusted LIBOR as the benchmark interest rate on the debt being hedged through its term. No credit spread was hedged. The Company designates its interest rate swap instruments as cash flow hedges.

The authoritative guidance requires companies to recognize derivative instruments as either an asset or liability measured at fair value in the statement of financial position. The effective portion of the change in fair value of the derivative instrument is recorded in other comprehensive income. The ineffective portion of the change in fair value of the derivative instrument, if any, is recognized in interest expense in the period of change. From the inception of the hedging program, the Company has determined that the hedging instruments are highly effective.

Foreign Exchange Contracts

The Company conducts business in a currency other than the U.S. dollar, associated with its international subsidiary in India. As a result, India s forecasted expenditures expose the Company to foreign currency risk. To mitigate this risk, the Company enters into derivative financial instruments, principally forward contracts, which are designated as cash flow hedges to mitigate fluctuations in the cash payments of future forecasted transactions in Indian rupees for up to 24 months. The Company adjusts the level and use of derivatives as soon as practicable after learning that an exposure has changed and the Company reviews all exposures and derivative positions on an ongoing basis.

Gains and losses on cash flow hedges are recorded in accumulated other comprehensive income (loss) until the hedged transaction is recorded in the consolidated financial statements. Once the underlying transaction is recorded in the consolidated financial statements, the Company reclassifies the accumulated gain or loss on the derivative into earnings. If all or a portion of the forecasted transaction was 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 June 30, 2010, the total notional amount of the forward contracts to buy Indian rupees in exchange for U.S. dollars was $13.3 million. All outstanding contracts qualified for hedge accounting treatment as of June 30, 2010. The Company estimates that approximately $0.1 million of net derivative loss 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 three and six months ended June 30, 2010.

The Company does not enter into derivative instruments for trading or speculative purposes.

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

	June 30, 2010		**December 31, 2009**	
	Balance Sheet Location	**Fair Value**	**Balance Sheet Location**	**Fair Value**
Derivatives designated as hedging instruments:				
Interest rate swaps	Other liabilities	$ 946	Other liabilities	$ 1,791
Foreign exchange contracts	Other liabilities	$ 120	Other liabilities	$ 245

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The following tables summarize the effects of derivatives in cash flow hedging relationships on the Company s statements of income for the three and six months ended June 30, 2010 and 2009 *(in thousands):*

	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 June 30,			Three Months Ended June 30,			Three Months Ended June 30,	
	2010	2009		2010	2009		2010	2009
Interest rate swaps	$ 374	$ 528	Interest expense	$	$	Other (expense) income	$	$
Foreign exchange contracts	$ (381)	$	Salaries and employee benefits	$ 9	$	Other (expense) income	$	$
Foreign exchange contracts	$ (78)	$	General and administrative expenses	$ 3	$	Other (expense) income	$	$

	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	
	Six Months Ended June 30,			Six Months Ended June 30,			Six Months Ended June 30,	
	2010	2009		2010	2009		2010	2009
Interest rate swaps	$ 845	$ 835	Interest expense	$	$	Other (expense) income	$	$
Foreign exchange contracts	$ 113	$	Salaries and employee benefits	$ 12	$	Other (expense) income	$	$
Foreign exchange contracts	$ 26	$	General and administrative expenses	$ 2	$	Other (expense) income	$	$

Note 5: Stock-Based Compensation

On March 9, 2009, the Board of Directors approved an amendment and restatement of the 2005 Stock Incentive Plan (2005 Plan), which was originally adopted on March 30, 2005, for Board members, employees, officers, and executives of, and consultants and advisors to, the Company. The amendment and restatement of the 2005 Plan increased by 2,000,000 shares the maximum number of shares of the Company s common stock that may be issued or be subject to awards under the plan, established a new 10-year term for the plan and made certain other amendments. The 2005 Plan amendment was approved by the Company s stockholders on June 9, 2009. The 2005 Plan provides for the granting of incentive stock options, nonqualified stock options, stock appreciation rights, restricted stock, restricted stock units, and performance-based awards to eligible individuals. As amended, the 2005 Plan allows the granting of an aggregate of 3,500,000 shares of the Company s common stock for awards, plus the number of shares of stock that were available for future awards under the prior 1999 Equity Participation Plan (1999 Plan). In addition, shares subject to options granted under either the 1999 Plan or the 2005 Plan that terminate or expire without being exercised will become available for grant under the 2005 Plan. The benefits provided under these plans are compensation subject to authoritative guidance for stock-based compensation.

In accordance with authoritative guidance for stock-based compensation, compensation expense is recognized only for those shares expected to vest, based on the Company s historical experience and future expectations. Total compensation expense during the six months ended June 30, 2010 and 2009 was $3.2 million and $2.1 million, respectively.

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The Company s stock-based compensation arrangements are described below:

Stock Options

The 2005 Plan permits the granting of stock options to employees, officers and executives, and directors of, and consultants and advisors to, the Company. The Company uses the Black-Scholes option-pricing model to determine the fair-value of stock-based awards. All options are amortized ratably over the requisite service periods of the awards, which are generally the vesting periods.

The fair value for options granted was estimated at the date of grant using a Black-Scholes option-pricing model with the following weighted-average assumptions:

	Six Months Ended June 30,	
	2010	**2009**
Weighted average fair value of options granted	$ 9.70	$ 1.36
Risk free interest rate	2.3%	1.9%
Dividend yield	0.0%	0.0%
Volatility factor of the expected market price of the Company s common stock	62.0%	52.8%
Weighted-average expected life of options	5 Years	5 Years

Unrecognized compensation cost related to stock options as of June 30, 2010 was $4.3 million. The weighted-average remaining expense period, based on the unamortized value of these outstanding stock options was approximately 2.3 years.

A summary of the Company s stock option activity as of June 30, 2010, and changes during the six months then ended, is presented below:

	Number of Shares	**Option Price Per Share**		**Weighted Average Exercise Price**	**Aggregate Intrinsic Value** *(in thousands)*
Outstanding at December 31, 2009	2,667,137	$ 0.35	$20.09	$ 9.28	
Granted	215,000		17.90	17.90	
Cancelled/forfeited	(39,333)	2.89	17.90	11.13	
Exercised	(242,038)	0.35	16.19	6.97	
Outstanding at June 30, 2010	2,600,766	$ 0.35	$20.09	$ 10.18	$ 27,129
Exercisable at June 30, 2010	1,518,487	$ 0.35	$20.09	$ 8.95	$ 17,708

The total intrinsic value of options exercised during the six months ended June 30, 2010 and 2009 was $3.2 million and $0.1 million, respectively. As of June 30, 2010, the weighted-average remaining contractual life of options outstanding and options exercisable was 6.3 years and 4.5 years, respectively.

Non-Vested Shares

Under the Company s 2005 Plan, employees, officers and executives and directors of, and consultants and advisors to, the Company are eligible to receive restricted stock units and restricted stock awards. In accordance with the authoritative guidance, the fair value of these non-vested shares is equal to the closing sale price of the Company s common stock on the date of issuance. The total number of these awards expected to vest is adjusted by estimated forfeiture rates. As of June 30, 2010, 88,825 of the non-vested shares are expected to vest over approximately one to two years based on certain performance goals (Performance-Based Awards). The fair value of the Performance-Based Awards is expensed over the expected vesting period, net of estimated forfeitures. If performance goals are not expected to be met, the compensation expense previously recognized would be reversed. No reversals of compensation expense related to the Performance-Based Awards have been made as

of June 30, 2010. The remaining 718,482 non-vested shares are not performance-based, and will vest over approximately one to five years of continuous service.

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A summary of the status of the Company s non-vested shares as of June 30, 2010, and changes during the six months then ended, is presented below:

Non-Vested Shares	Non-Vested Shares	Weighted Average Grant Date Fair Value
Non-vested at December 31, 2009	675,790	$ 9.27
Awarded	335,169	$ 17.81
Vested	(184,987)	$ 9.85
Cancelled/forfeited	(18,665)	$ 11.33
Non-vested at June 30, 2010	807,307	$ 12.63

Unrecognized compensation expense related to non-vested shares as of June 30, 2010, was $5.9 million. The weighted-average remaining expense period, based on the unamortized value of these outstanding non-vested shares was approximately 2.5 years. The fair value of vested shares during the six months ended June 30, 2010 and 2009 was $3.5 million and $1.0 million, respectively.

Note 6: 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 a quarter are aggregated into pools based on common risk characteristics. 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 consumer receivable portfolios using either the interest method or the cost recovery method. The interest method applies an effective interest rate, or 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 generally 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 income as a reduction in revenue, with a corresponding valuation allowance, offsetting the investment in receivable portfolios in the consolidated statements of financial condition.

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 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 income 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.

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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 current period *(in thousands)*:

	Accretable Yield	Estimate of Zero Basis Cash Flows	Total
Balance at December 31, 2009	$ 628,439	$ 4,695	$ 633,134
Revenue recognized, net	(80,851)	(2,056)	(82,907)
Net additions to existing portfolios	45,179	1,702	46,881
Additions for current purchases	93,430		93,430
Balance at March 31, 2010	$ 686,197	$ 4,341	$ 690,538
Revenue recognized, net	(89,490)	(2,355)	(91,845)
Additions to existing portfolios	16,481	1,960	18,441
Additions for current purchases	95,862		95,862
Balance at June 30, 2010	$ 709,050	$ 3,946	$ 712,996

	Accretable Yield	Estimate of Zero Basis Cash Flows	Total
Balance at December 31, 2008	$ 592,825	$ 8,337	$ 601,162
Revenue recognized, net	(69,775)	(2,500)	(72,275)
Net additions to existing portfolios	5,715	1,032	6,747
Additions for current purchases	81,917		81,917
Balance at March 31, 2009	610,682	6,869	617,551
Revenue recognized, net	(71,576)	(2,389)	(73,965)
(Reductions) additions to existing portfolios	(15,399)	2,614	(12,785)
Additions for current purchases	106,771		106,771
Balance at June 30, 2009	$ 630,478	$ 7,094	$ 637,572

During the three months ended June 30, 2010, the Company purchased receivable portfolios with a face value of $2.2 billion for $83.3 million, or a purchase cost of 3.7% of face value. The estimated future collections at acquisition for these portfolios amounted to $174.5 million. During the six months ended June 30, 2010, the Company purchased receivable portfolios with a face value of $4.4 billion for $165.0 million, or a purchase cost of 3.8% of face value. The estimated future collections at acquisition for these portfolios amounted to $347.8 million.

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). Zero Basis Revenue remained consistent at $2.4 million during the three months ended June 30, 2010 and 2009. During the six months ended June 30, 2010 and 2009, approximately $4.4 million and $4.9 million were recognized as Zero Basis Revenue, respectively.

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 June 30, 2010	
	Total

	Accrual Basis Portfolios	Cost Recovery Portfolios	Zero Basis Portfolios	
Balance, beginning of period	$ 549,180	$ 480	$	$ 549,660
Purchases of receivable portfolios	83,336			83,336
Gross collections[1]	(154,367)	(24)	(2,355)	(156,746)
Put-backs and recalls[2]	(1,280)			(1,280)
Revenue recognized[3]	92,329		2,355	94,684
Portfolio allowances, net	(2,383)	(456)		(2,839)
Balance, end of period	$ 566,815	$	$	$ 566,815
Revenue as a percentage of collections[4]	59.8%	0.0%	100.0%	60.4%

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	Three Months Ended June 30, 2009			
	Accrual Basis Portfolios	Cost Recovery Portfolios	Zero Basis Portfolios	Total
Balance, beginning of period	$ 472,875	$ 609	$	$ 473,484
Purchases of receivable portfolios	82,033			82,033
Gross collections[1]	(119,823)	(56)	(2,389)	(122,268)
Put-backs and recalls[2]	(506)			(506)
Revenue recognized[3]	76,172		2,357	78,529
(Portfolio allowances) portfolio allowance reversals, net	(4,596)		32	(4,564)
Balance, end of period	$ 506,155	$ 553	$	$ 506,708
Revenue as a percentage of collections[4]	63.6%	0.0%	98.7%	64.2%

	Six Months Ended June 30, 2010			
	Accrual Basis Portfolios	Cost Recovery Portfolios	Zero Basis Portfolios	Total
Balance, beginning of period	$ 526,366	$ 511	$	$ 526,877
Purchases of receivable portfolios	164,968			164,968
Gross collections[1]	(293,451)	(55)	(4,412)	(297,918)
Put-backs and recalls[2]	(1,864)			(1,864)
Revenue recognized[3]	181,061		4,411	185,472
(Portfolio allowances) portfolio allowance reversals, net	(10,265)	(456)	1	(10,720)
Balance, end of period	$ 566,815	$	$	$ 566,815
Revenue as a percentage of collections[4]	61.7%	0.0%	100.0%	62.3%

	Six Months Ended June 30, 2009			
	Accrual Basis Portfolios	Cost Recovery Portfolios	Zero Basis Portfolios	Total
Balance, beginning of period	$ 460,598	$ 748	$	$ 461,346
Purchases of receivable portfolios	137,946			137,946
Gross collections[1]	(232,314)	(195)	(4,885)	(237,394)
Put-backs and recalls[2]	(1,426)		(4)	(1,430)
Revenue recognized[3]	151,374		4,857	156,231
(Portfolio allowances) portfolio allowance reversals, net	(10,023)		32	(9,991)
Balance, end of period	$ 506,155	$ 553	$	$ 506,708
Revenue as a percentage of collections[4]	65.2%	0.0%	99.4%	65.8%

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

(3) Includes retained interest.

(4) 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 June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
Balance at beginning of period	$ 84,343	$ 62,579	$ 76,462	$ 57,152
Provision for portfolio allowances	4,659	4,722	14,389	10,302
Reversal of prior allowance	(1,820)	(158)	(3,669)	(311)
Balance at end of period	$ 87,182	$ 67,143	$ 87,182	$ 67,143

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The Company currently utilizes various business channels for the collection of its receivables. The following table summarizes the collections by collection channel *(in thousands)*:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
Collection sites	$ 66,619	$ 44,680	$ 132,424	$ 95,022
Legal collections	68,049	61,460	125,222	117,867
Collection agencies	21,960	15,506	39,712	23,173
Sales and other				