

CONSUMER PORTFOLIO SERVICES INC
Form 10-Q
August 09, 2013

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2013

Commission file number: 1-11416

CONSUMER PORTFOLIO SERVICES, INC.

(Exact name of registrant as specified in its charter)

California 33-0459135
(State or other jurisdiction of incorporation or organization) (IRS Employer Identification No.)

19500 Jamboree Road, Irvine, California 92612
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including Area Code: (949) 753-6800

Former name, former address and former fiscal year, if changed since last report: N/A

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

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

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

Large Accelerated Filer Accelerated Filer
Non-Accelerated Filer Smaller Reporting Company

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

As of August 2, 2013 the registrant had 21,604,739 common shares outstanding.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES

INDEX TO FORM 10-Q

For the Quarterly Period Ended June 30, 2013

	<u>Page</u>
PART I. FINANCIAL INFORMATION	
Item 1. Financial Statements	3
Unaudited Condensed Consolidated Balance Sheets as of June 30, 2013 and December 31, 2012	3
Unaudited Condensed Consolidated Statements of Operations for the three-month and six-month periods ended June 30, 2013 and 2012	4
Unaudited Condensed Consolidated Statements of Comprehensive Income for the three-month and six-month periods ended June 30, 2013 and 2012	5
Unaudited Condensed Consolidated Statements of Cash Flows for the six-month periods ended June 30, 2013 and 2012	6
Notes to Unaudited Condensed Consolidated Financial Statements	7
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	24
Item 4. Controls and Procedures	45
PART II. OTHER INFORMATION	
Item 1. Legal Proceedings	46
Item 1A. Risk Factors	46
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds	48
Item 6. Exhibits	48
Signatures	49

PART I. FINANCIAL INFORMATION**Item 1. Financial Statements****CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES****UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS****(In thousands, except share and per share data)**

	June 30, 2013	December 31, 2012
ASSETS		
Cash and cash equivalents	\$18,584	\$12,966
Restricted cash and equivalents	122,864	104,445
Finance receivables	971,914	764,343
Less: Allowance for finance credit losses	(32,101)	(19,594)
Finance receivables, net	939,813	744,749
Finance receivables measured at fair value	30,319	59,668
Residual interest in securitizations	2,246	4,824
Furniture and equipment, net	546	726
Deferred financing costs	11,184	9,140
Deferred tax assets, net	69,971	75,640
Accrued interest receivable	12,905	10,411
Other assets	16,608	15,051
	\$1,225,040	\$1,037,620
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities		
Accounts payable and accrued expenses	\$29,672	\$17,785
Warehouse lines of credit	17,144	21,731
Residual interest financing	33,773	13,773
Debt secured by receivables measured at fair value	25,622	57,107
Securitization trust debt	983,887	792,497
Senior secured debt, related party	39,368	50,135
Subordinated renewable notes	22,569	23,281
	1,152,035	976,309
COMMITMENTS AND CONTINGENCIES		
Shareholders' Equity		

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Preferred stock, \$1 par value; authorized 4,998,130 shares; none issued	–	–
Series A preferred stock, \$1 par value; authorized 5,000,000 shares; none issued	–	–
Series B preferred stock, \$1 par value; authorized 1,870 shares; none issued	–	–
Common stock, no par value; authorized 75,000,000 shares; 21,361,239 and 19,838,913 shares issued and outstanding at June 30, 2013 and December 31, 2012, respectively	68,762	65,678
Retained earnings	9,880	1,270
Accumulated other comprehensive loss	(5,637)	(5,637)
	73,005	61,311
	\$1,225,040	\$1,037,620

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(In thousands, except per share data)**

	Three Months Ended		Six Months Ended	
	June 30, 2013	2012	June 30, 2013	2012
Revenues:				
Interest income	\$55,797	\$41,546	\$106,964	\$82,157
Servicing fees	876	595	1,784	1,396
Other income	2,862	2,010	5,380	5,116
Gain on cancellation of debt	10,947	–	10,947	–
	70,482	44,151	125,075	88,669
Expenses:				
Employee costs	11,527	8,277	20,476	17,148
General and administrative	4,518	3,577	8,272	8,075
Interest	14,601	19,827	30,947	42,136
Provision for credit losses	17,371	7,711	32,519	12,547
Provision for contingent liabilities	9,650	–	9,650	–
Marketing	3,472	2,560	6,654	5,180
Occupancy	683	726	1,226	1,447
Depreciation and amortization	114	132	257	284
	61,936	42,810	110,001	86,817
Income before income tax expense	8,546	1,341	15,074	1,852
Income tax expense	3,721	–	6,464	–
Net income	\$4,825	\$1,341	\$8,610	\$1,852
Earnings per share:				
Basic	\$0.23	\$0.07	\$0.42	\$0.10
Diluted	0.15	0.05	0.27	0.08
Number of shares used in computing earnings per share:				
Basic	20,989	19,305	20,534	19,360
Diluted	31,788	24,636	31,709	23,283

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Net income	\$4,825	\$1,341	\$8,610	\$1,852
Other comprehensive income/(loss); change in funded status of pension plan	–	–	–	–
Comprehensive income	\$4,825	\$1,341	\$8,610	\$1,852

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(In thousands)**

	Six Months Ended June 30,	
	2013	2012
Cash flows from operating activities:		
Net income	\$8,610	\$1,852
Adjustments to reconcile net income to net cash provided by operating activities:		
Accretion of deferred acquisition fees	(10,309)	(7,169)
Accretion of purchase discount on receivables measured at fair value	(984)	(5,049)
Amortization of discount on securitization trust debt	502	917
Amortization of discount on senior secured debt, related party	1,370	1,567
Accretion of premium on debt secured by receivables measured at fair value	1,556	5,108
Mark to fair value on debt secured by receivables measured at fair value	(497)	6,015
Mark to fair value of receivables measured at fair value	613	(5,217)
Depreciation and amortization	257	284
Amortization of deferred financing costs	1,196	1,865
Provision for credit losses	32,519	12,547
Provision for contingent liabilities	9,650	-
Stock-based compensation expense	1,820	618
Interest income on residual assets	-	(436)
Gain on cancellation of debt	(10,947)	-
Changes in assets and liabilities:		
Accrued interest receivable	(2,494)	(848)
Deferred tax assets, net	5,669	-
Other assets	(977)	35
Accounts payable and accrued expenses	2,819	(3,169)
Net cash provided by operating activities	40,373	8,920
Cash flows from investing activities:		
Purchases of finance receivables held for investment	(383,898)	(257,800)
Payments received on finance receivables held for investment	166,625	153,993
Payments on receivables portfolio at fair value	29,720	68,153
Proceeds received on residual interest in securitizations	2,578	-
Change in repossessions held in inventory	(580)	464
Decreases (increases) in restricted cash and cash equivalents, net	(18,419)	31,422
Purchase of furniture and equipment	(77)	(176)
Net cash provided by (used in) investing activities	(204,051)	(3,944)
Cash flows from financing activities:		
Proceeds from issuance of securitization trust debt	390,000	296,500
Proceeds from issuance of subordinated renewable notes	1,027	1,576

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Payments on subordinated renewable notes	(1,739)	(1,226)
Net proceeds from (repayments of) warehouse lines of credit	(4,587)	3,175
Proceeds from (repayments of) residual interest financing debt	20,000	(6,563)
Repayment of securitization trust debt	(188,165)	(214,405)
Repayment of debt secured by receivables measured at fair value	(32,544)	(73,289)
Repayment of senior secured debt, related party	(12,137)	(6,200)
Payment of financing costs	(3,240)	(4,064)
Repurchase of common stock	(1,138)	(435)
Exercise of options and warrants	1,819	101
Net cash provided by (used in) financing activities	169,296	(4,830)
Increase in cash and cash equivalents	5,618	146
Cash and cash equivalents at beginning of period	12,966	10,094
Cash and cash equivalents at end of period	\$ 18,584	\$ 10,240
Supplemental disclosure of cash flow information:		
Cash paid (received) during the period for:		
Interest	\$ 25,612	\$ 43,288
Income taxes	\$ 1,695	\$ 745
Non-cash financing activities:		
Derivative warrants reclassified from accounts payable to common stock	\$ 583	\$ 1,358

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(1) Summary of Significant Accounting Policies

Description of Business

We were formed in California on March 8, 1991. We specialize in purchasing and servicing retail automobile installment sale contracts (“automobile contracts” or “finance receivables”) originated by licensed motor vehicle dealers located throughout the United States (“dealers”) in the sale of new and used automobiles, light trucks and passenger vans. Through our purchases, we provide indirect financing to dealer customers for borrowers with limited credit histories, low incomes or past credit problems (“sub-prime customers”). We serve as an alternative source of financing for dealers, allowing sales to customers who otherwise might not be able to obtain financing. In addition to purchasing installment purchase contracts directly from dealers, we have also (i) acquired installment purchase contracts in four merger and acquisition transactions, (ii) purchased immaterial amounts of vehicle purchase money loans from non-affiliated lenders, and (iii) lent money directly to consumers for an immaterial amount of loans secured by vehicles. In this report, we refer to all of such contracts and loans as “automobile contracts.”

Basis of Presentation

Our Unaudited Condensed Consolidated Financial Statements have been prepared in conformity with accounting principles generally accepted in the United States of America, with the instructions to Form 10-Q and with Article 8 of Regulation S-X of the Securities and Exchange Commission, and include all adjustments that are, in management’s opinion, necessary for a fair presentation of the results for the interim periods presented. All such adjustments are, in the opinion of management, of a normal recurring nature. Results for the six-month period ended June 30, 2013 are not necessarily indicative of the operating results to be expected for the full year.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted from these Unaudited Condensed Consolidated Financial Statements. These Unaudited Condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and Notes to Consolidated Financial Statements included in our Annual Report on Form 10-K for the year ended December 31, 2012.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements, as well as the reported amounts of income and expenses during the reported periods. Specifically, a number of estimates were made in connection with determining an appropriate allowance for finance credit losses, valuing finance receivables measured at fair value and the related debt, valuing residual interest in securitizations, accreting net acquisition fees, amortizing deferred costs, valuing stock options and warrants issued, and recording deferred tax assets and reserves for uncertain tax positions. These are material estimates that could be susceptible to changes in the near term and, accordingly, actual results could differ from those estimates.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****Other Income**

The following table presents the primary components of Other Income for the three-month and six-month periods ending June 30, 2013 and 2012:

	Three Months Ended June 30, 2013 2012 (In thousands)		Six Months Ended June 30, 2013 2012 (In thousands)	
Direct mail revenues	\$1,963	\$1,232	\$3,727	\$2,851
Convenience fee revenue	828	690	1,515	1,522
Recoveries on previously charged-off contracts	54	148	104	245
Sales tax refunds	–	55	84	127
Other	17	(115)	(50)	371
Other income for the period	\$2,862	\$2,010	\$5,380	\$5,116

Stock-based Compensation

We recognize compensation costs in the financial statements for all share-based payments based on the grant date fair value estimated in accordance with the provisions of ASC 718 “Stock Compensation”.

For the six months ended June 30, 2013 and 2012, we recorded stock-based compensation costs in the amount of \$1,820,000 and \$618,000, respectively. As of June 30, 2013, unrecognized stock-based compensation costs to be recognized over future periods equaled \$14.6 million. This amount will be recognized as expense over a weighted-average period of 3.6 years.

The following represents stock option activity for the six months ended June 30, 2013:

	Number of Shares (in thousands)	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term
Options outstanding at the beginning of period	8,652	\$ 1.58	N/A
Granted	3,025	7.43	N/A
Exercised	(394)	1.73	N/A
Forfeited	–	–	N/A
Options outstanding at the end of period	11,283	\$ 3.15	6.82 years
Options exercisable at the end of period	6,174	\$ 1.69	4.97 years

At June 30, 2013, the aggregate intrinsic value of options outstanding and exercisable was \$48.3 million and \$34.9 million, respectively. There were 394,000 options exercised for the six months ended June 30, 2013 compared to 87,000 for the comparable period in 2012. There were 3.9 million shares available for future stock option grants under existing plans as of June 30, 2013.

Purchases of Company Stock

During the six-month period ended June 30, 2013 and 2012, we purchased 118,544 and 320,154 shares, respectively, of our common stock, at average prices of \$9.60 and \$1.36, respectively.

Reclassifications

Some items in the prior year financial statements were reclassified to conform to the current presentation. Reclassifications had no effect on prior year net income or total shareholders' equity.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Derivative Financial Instruments

We do not use derivative financial instruments to hedge exposures to cash flow or market risks. However, from 2008 to 2010, we issued warrants to purchase the Company's common stock in conjunction with various debt financing transactions. At the time of issuance, five of these warrants issued contained "down round," or price reset, features that are subject to classification as liabilities for financial statement purposes. These liabilities were measured at fair value, with the changes in fair value at the end of each period reflected as current period income or loss. Accordingly, changes to the market price per share of our common stock underlying these warrants with "down round," or price reset, features directly affected the fair value computations for these derivative financial instruments. The effect was that any increase in the market price per share of our common stock would also increase the related liability, which in turn would result in a current period loss. Conversely, any decrease in the market price per share of our common stock would also decrease the related liability, which in turn would result in a current period gain. We used a binomial pricing model to compute the fair value of the liabilities associated with the outstanding warrants. In computing the fair value of the warrant liabilities at the end of each period, we used significant judgments with respect to the risk free interest rate, the volatility of our stock price, and the estimated life of the warrants. The warrant liabilities were included in Accounts payable and accrued expenses on our consolidated balance sheets. On March 29, 2012 we agreed with the holders to amend three of the five warrants that contained the "down round" features, removing those specific price reset terms. On the date of the amendment, we valued each of the three warrants using a binomial pricing model as described above. The aggregate value of the three amended warrants of \$1.1 million was then reclassified from Accounts payable to Common Stock. On June 25, 2012 we agreed with the holder to amend one other warrant that contained the "down round" features, removing those specific price reset terms. The \$250,000 aggregate value of this amended warrant was reclassified from Accounts payable to Common stock on the date of the amendment. The fifth warrant with the "down round" feature was exercised on February 22, 2013. The \$583,000 intrinsic value of this warrant was reclassified from Accounts payable to Common stock on the date of the exercise. As of June 30, 2013 all five of the warrants issued that previously contained price reset features have either been amended or exercised and are no longer subject to quarterly valuations.

Financial Covenants

Certain of our securitization transactions, our warehouse credit facilities and our residual interest financing contain various financial covenants requiring minimum financial ratios and results. Such covenants include maintaining minimum levels of liquidity and net worth and not exceeding maximum leverage levels. As of June 30, 2013, we were in compliance with all such covenants. In addition, certain securitization and non-securitization related debt agreements contain cross-default provisions that would allow certain creditors to declare a default if a default occurred under a different facility.

Finance Receivables and Related Debt Measured at Fair Value

In September 2011 we purchased approximately \$217.8 million of finance receivables from Fireside Bank. These receivables and the related acquisition debt are recorded on our balance sheet at fair value. There are no level 1 or level 2 inputs (as described by ASC 820) available to us for measurement of such receivables, or for the related debt. Our level 3, unobservable inputs reflect our own assumptions about the factors that market participants use in pricing similar receivables and debt, and are based on the best information available in the circumstances. The valuation method used to estimate fair value may produce a fair value measurement that may not be indicative of ultimate realizable value. Furthermore, while we believe our valuation methods are appropriate and consistent with those used by other market participants, the use of different methods or assumptions to estimate the fair value of certain financial instruments could result in different estimates of fair value. Those estimated values may differ significantly from the values that would have been used had a readily available market for such receivables or debt existed, or had such receivables or debt been liquidated, and those differences could be material to the financial statements.

Gain on Cancellation of Debt

In April 2013, we repurchased the outstanding Class D notes from our first 2008 securitization for a cash payment of \$6.1 million and a new 5% note for \$5.3 million due in June 2014. The Class D notes were held by the same related party that holds our senior secured debt. On the date we repurchased the Class D Notes, the Class D noteholder owned 10.5% of our outstanding common stock. We subsequently exercised our “clean-up call” option and repurchased the remaining collateral from the related securitization trust. The aggregate value of our consideration for the Class D notes was \$10.9 million less than our carrying value of the Class D notes at the time of the repurchase. As a result of the repurchase of the Class D notes and the termination of the securitization trust, we realized a gain of \$10.9 million.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****Provision for Contingent Liabilities**

In June 30, 2013, we recognized \$9.7 million in contingent liability expenses to either record or increase the amounts we believe represents our best estimate of probable incurred losses related to various pending litigation. The amount was allocated in part to a long running case we refer to as the Stanwich litigation, and also to more recent matters including two California class action suits where we are the defendant, and a governmental inquiry, in which the United States Federal Trade Commission (“FTC”) has informally proposed that the we refrain from certain allegedly unfair trade practices, and to make restitutionary payments into a consumer relief fund.

(2) Finance Receivables

Our portfolio of finance receivables consists of small-balance homogeneous contracts comprising a single segment and class that is collectively evaluated for impairment on a portfolio basis according to delinquency status. Our contract purchase guidelines are designed to produce a homogenous portfolio. For key terms such as interest rate, length of contract, monthly payment and amount financed, there is relatively little variation from the average for the portfolio. We report delinquency on a contractual basis. Once a contract becomes greater than 90 days delinquent, we do not recognize additional interest income until the obligor under the contract makes sufficient payments to be less than 90 days delinquent. Any payments received on a contract that is greater than 90 days delinquent are first applied to accrued interest and then to principal reduction.

The following table presents the components of Finance Receivables, net of unearned interest:

	June 30, 2013	December 31, 2012
Finance Receivables	(In thousands)	
Automobile finance receivables, net of unearned interest	\$ 1,004,141	\$ 795,786
Less: Unearned acquisition fees and originations costs	(32,227)	(31,443)
Finance Receivables	\$ 971,914	\$ 764,343

We consider an automobile contract delinquent when an obligor fails to make at least 90% of a contractually due payment by the following due date, which date may have been extended within limits specified in the servicing agreements. The period of delinquency is based on the number of days payments are contractually past due, as extended where applicable. Automobile contracts less than 31 days delinquent are not included. In certain circumstances we will grant obligors one-month payment extensions to assist them with temporary cash flow problems. The only modification of terms is to advance the obligor's next due date by one month and extend the maturity date of the receivable by one month. In some cases, a two-month extension may be granted. There are no other concessions such as a reduction in interest rate, forgiveness of principal or of accrued interest. Accordingly, we consider such extensions to be insignificant delays in payments rather than troubled debt restructurings. The following table summarizes the delinquency status of finance receivables as of June 30, 2013 and December 31, 2012:

	June 30, 2013	December 31, 2012
	(In thousands)	
Delinquency Status		
Curent	\$966,412	\$764,741
31 – 60 days	20,887	16,925
61 – 90 days	11,409	9,019
91 + days	5,433	5,101
	\$1,004,141	\$795,786

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

Finance receivables totaling \$5.4 million and \$5.1 million at June 30, 2013 and December 31, 2012, respectively, including all receivables greater than 90 days delinquent, have been placed on non-accrual status as a result of their delinquency status.

We use a loss allowance methodology commonly referred to as "static pooling," which stratifies our finance receivable portfolio into separately identified pools based on the period of origination. Using analytical and formula driven techniques, we estimate an allowance for finance credit losses, which we believe is adequate for probable credit losses that can be reasonably estimated in our portfolio of automobile contracts. The estimate for probable credit losses is reduced by our estimate for future recoveries on previously incurred losses. Provision for losses is charged to our consolidated statement of operations. Net losses incurred on finance receivables are charged to the allowance. For finance receivables originated through December 31, 2010 we established the allowance at the time of the acquisition of the receivable. Beginning January 1, 2011, we establish the allowance for new receivables over the 12-month period following their acquisition.

The following table presents a summary of the activity for the allowance for finance credit losses for the three-month and six-month periods ended June 30, 2013 and 2012:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(In thousands)		(In thousands)	
Balance at beginning of period	\$24,881	\$11,251	\$19,594	\$10,351
Provision for credit losses on finance receivables	17,371	7,711	32,519	12,547
Charge-offs	(13,361)	(8,278)	(26,277)	(16,580)
Recoveries	3,210	3,409	6,265	7,775
Balance at end of period	\$32,101	\$14,093	\$32,101	\$14,093

Excluded from finance receivables are contracts that were previously classified as finance receivables but were reclassified as other assets because we have repossessed the vehicle securing the Contract. The following table presents a summary of such repossessed inventory together with the allowance for losses in repossessed inventory that is not included in the allowance for finance credit losses:

	June 30, 2013	December 31, 2012
	(In thousands)	
Gross balance of repossessions in inventory	\$ 13,839	\$ 12,102
Allowance for losses on repossessed inventory	(7,541)	(6,384)
Net repossessed inventory included in other assets	\$ 6,298	\$ 5,718

(3) Finance Receivables Measured at Fair Value

In September 2011 we purchased approximately \$217.8 million of finance receivables from Fireside Bank. These receivables are recorded on our balance sheet at fair value.

The following table presents the components of Finance Receivables measured at fair value:

	June 30, 2013	December 31, 2012
	(In thousands)	
Finance Receivables Measured at Fair Value		
Finance receivables and accrued interest, net of unearned interest	\$ 31,084	\$ 60,804
Less: Fair value adjustment	(765)	(1,136)
Finance receivables measured at fair value	\$ 30,319	\$ 59,668

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

The following table summarizes the delinquency status of finance receivables measured at fair value as of June 30, 2013 and December 31, 2012:

	June 30, 2013	December 31, 2012
(In thousands)		
Delinquency Status		
Curent	\$29,228	\$ 57,557
31 – 60 days	1,309	2,206
61 – 90 days	399	710
91 + days	148	331
	\$31,084	\$ 60,804

(4) Securitization Trust Debt

We have completed a number of securitization transactions that are structured as secured borrowings for financial accounting purposes. The debt issued in these transactions is shown on our Unaudited Condensed Consolidated Balance Sheets as “Securitization trust debt,” and the components of such debt are summarized in the following table:

Series	Final Scheduled Payment Date (1)	Receivables Pledged at June 30, 2013	Initial Principal	Outstanding Principal at June 30, 2013	Outstanding Principal at December 31, 2012	Weighted Average Contractual Interest Rate at June 30, 2013
(Dollars in thousands)						
CPS 2008-A	October 2014	\$ –	\$310,359	\$ –	\$ 40,713	–
Page Five Funding	January 2018	15,902	46,058	14,631	21,251	9.42%
CPS 2011-A	April 2018	38,441	100,364	35,026	48,368	3.70%
CPS 2011-B	September 2018	57,385	109,936	57,535	70,863	4.72%
CPS 2011-C	March 2019	71,483	119,400	71,437	88,269	5.05%

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CPS 2012-A	June 2019	82,727	155,000	82,751	105,485	3.61%
CPS 2012-B	September 2019	107,205	141,500	103,442	122,329	3.19%
CPS 2012-C	December 2019	115,057	147,000	110,018	135,219	2.51%
CPS 2012-D	March 2020	137,136	160,000	131,283	160,000	2.07%
CPS 2013-A	June 2020	176,266	185,000	172,764	–	1.80%
CPS 2013-B	September 2020	138,512	205,000	205,000	–	2.24%
		\$ 940,114	\$ 1,679,617	\$ 983,887	\$ 792,497	

The Final Scheduled Payment Date represents final legal maturity of the securitization trust debt. Securitization trust debt is expected to become due and to be paid prior to those dates, based on amortization of the finance (1)receivables pledged to the trusts. Expected payments, which will depend on the performance of such receivables, as to which there can be no assurance, are \$193.4 million in 2013, \$335.0 million in 2014, \$236.4 million in 2015, \$143.3 million in 2016, \$69.1 million in 2017 and \$6.7 million in 2018.

All of the securitization trust debt was sold in private placement transactions to qualified institutional buyers. The debt was issued through our wholly-owned bankruptcy remote subsidiaries and is secured by the assets of such subsidiaries, but not by our other assets.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The terms of the securitization agreements related to the issuance of the securitization trust debt and the warehouse credit facilities require that we meet certain delinquency and credit loss criteria with respect to the pool of receivables, and certain of the agreements require that we maintain minimum levels of liquidity and not exceed maximum leverage levels. In addition, certain securitization and non-securitization related debt contain cross-default provisions, which would allow certain creditors to declare a default if a default were declared under a different facility. As of June 30, 2013, we were in compliance with all such covenants.

We are responsible for the administration and collection of the automobile contracts. The securitization agreements also require certain funds be held in restricted cash accounts to provide additional collateral for the borrowings, to be applied to make payments on the securitization trust debt or as pre-funding proceeds from a term securitization prior to the purchase of additional collateral. As of June 30, 2013, restricted cash under the various agreements totaled approximately \$122.9 million. Interest expense on the securitization trust debt consists of the stated rate of interest plus amortization of additional costs of borrowing. Additional costs of borrowing include facility fees, amortization of deferred financing costs and discounts on notes sold. Deferred financing costs and discounts on notes sold related to the securitization trust debt are amortized using a level yield method. Accordingly, the effective cost of the securitization trust debt is greater than the contractual rate of interest disclosed above.

Our wholly-owned bankruptcy remote subsidiaries were formed to facilitate the above asset-backed financing transactions. Similar bankruptcy remote subsidiaries issue the debt outstanding under our credit facilities. Bankruptcy remote refers to a legal structure in which it is expected that the applicable entity would not be included in any bankruptcy filing by its parent or affiliates. All of the assets of these subsidiaries have been pledged as collateral for the related debt. All such transactions, treated as secured financings for accounting and tax purposes, are treated as sales for all other purposes, including legal and bankruptcy purposes. None of the assets of these subsidiaries are available to pay other creditors.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(5) Debt

The terms and amounts of our other debt outstanding at June 30, 2013 and December 31, 2012 are summarized below:

Description	Interest Rate	Maturity	Amount Outstanding at	
			June 30, 2013	December 31, 2012
			(In thousands)	
Residual interest financing	12.875% over one month Libor	September 2013	\$13,773	\$13,773
	11.75% over one month Libor	April 2018	20,000	–
Senior secured debt, related party	13.0% and 16.0% at June 30, 2013 and December 31, 2012, respectively	June 2014	36,505	50,135
	5.00%	June 2014	2,863	–
Subordinated renewable notes	Weighted average rate of 13.2% and 14.4% at June 30, 2013 and December 31, 2012, respectively	Weighted average maturity of March 2016 and June 2015 at June 30, 2013 and December 31, 2012, respectively	22,569	23,281
Debt secured by receivables measured at fair value	8.00%	Repayment is based on payments from underlying receivables. Final payment of the 8.00% note is expected in September 2013, with residual payments extending through 2016	25,622	57,107
			\$121,332	\$144,296

On April 11, 2013 we entered into a new \$20 million five-year residual financing facility secured by eligible residual assets in two previously securitized pools of automobile receivables. On April 12, 2013, we prepaid \$15 million of our senior secured debt and reduced the interest rate on the remaining outstanding amount from 16.00% to 13.00%. The maturity date on the remaining outstanding amount was extended from December 2013 to June 2014.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS*****(6) Interest Income and Interest Expense***

The following table presents the components of interest income:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(In thousands)		(In thousands)	
Interest on Finance Receivables	\$55,796	\$41,076	\$106,954	\$81,221
Residual interest income	–	234	–	458
Other interest income	1	236	10	478
Interest income	\$55,797	\$41,546	\$106,964	\$82,157

The following table presents the components of interest expense:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(In thousands)		(In thousands)	
Securitization trust debt	\$8,230	\$9,139	\$17,368	\$19,159
Warehouse lines of credit	1,297	1,668	2,579	3,064
Senior secured debt, related party	2,112	3,259	4,875	6,796
Debt secured by receivables at fair value	1,027	4,297	2,813	10,087
Residual interest financing	1,094	646	1,586	1,394
Subordinated renewable notes	841	818	1,726	1,636
	\$14,601	\$19,827	\$30,947	\$42,136

(7) Earnings Per Share

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Earnings per share for the three-month and six-month periods ended June 30, 2013 and 2012 were calculated using the weighted average number of shares outstanding for the related period. The following table reconciles the number of shares used in the computations of basic and diluted earnings per share for the three-month and six-month periods ended June 30, 2013 and 2012:

	Six Months Ended June 30, 2013 2012 (In thousands)		Three Months Ended June 30, 2013 2012 (In thousands)	
Weighted average number of common shares outstanding during the period used to compute basic earnings per share	20,989	19,305	20,534	19,360
	\$			
Incremental common shares attributable to exercise of outstanding options and warrants	10,799	5,331	11,175	3,923
	\$			
Weighted average number of common shares used to compute diluted earnings per share	31,788	24,636	31,709	23,283

If the anti-dilutive effects of common stock equivalents were considered, shares included in the diluted earnings per share calculation for the three-month and six-month periods ended June 30, 2013 would have included an additional 2.2 million and 1.5 million shares, respectively, attributable to the exercise of outstanding options and warrants. For the three-month and six-month periods ended June 30, 2012, the anti-dilutive shares were 2.1 million and 7.2 million, respectively.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(8) *Income Taxes*

We file numerous consolidated and separate income tax returns with the United States and with many states. With few exceptions, we are no longer subject to U.S. federal, state, or local examinations by tax authorities for years before 2008.

We do not anticipate that total unrecognized tax benefits will significantly change due to any settlements of audits or expirations of statutes of limitations over the next 12 months.

The Company and its subsidiaries file a consolidated federal income tax return and combined or stand-alone state franchise tax returns for certain states. We utilize the asset and liability method of accounting for income taxes, under which deferred income taxes are recognized for the future tax consequences attributable to the differences between the financial statement values of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date.

Deferred tax assets are recognized subject to management's judgment that realization is more likely than not. A valuation allowance is recognized for a deferred tax asset if, based on the weight of the available evidence, it is more likely than not that some portion of the deferred tax asset will not be realized. In making such judgments, significant weight is given to evidence that can be objectively verified. As a result of the unprecedented adverse changes in the market for securitizations, the recession and the resulting high levels of unemployment that occurred in 2008 and 2009, we incurred substantial operating losses from 2009 through 2011 which led us to establish a valuation allowance against a substantial portion of our deferred tax assets. However, since the fourth quarter of 2011, we have reported seven consecutive quarters of increasing profitability, observed improvement in credit metrics, and produced reliable internal financial projections. Furthermore, we have demonstrated an ability to increase our volumes of contract purchases, grow our managed portfolio and obtain cost effective short and long-term financing for our finance receivables. As a result of these and other factors, we determined at December 31, 2012 that, based on the weight of the available objective evidence, it was more likely than not that we would generate sufficient future taxable income to utilize our net deferred tax assets. Accordingly, we reversed the related valuation allowance of \$62.8 million in the fourth quarter of 2012.

Although realization is not assured, we believe that the realization of the recognized net deferred tax asset of \$70.0 million as of June 30, 2013 is more likely than not based on forecasted future net earnings. Our net deferred tax asset of \$70.0 million consists of approximately \$57.7 million of net U.S. federal deferred tax assets and \$12.3 million of net state deferred tax assets. The major components of the deferred tax asset are \$50.9 million in net operating loss carryforwards and built in losses and \$19.1 million in net deductions which have not yet been taken on a tax return. We estimate that we would need to generate approximately \$175 million of taxable income during the applicable carryforward periods to realize fully our federal and state net deferred tax assets.

(9) Legal Proceedings

Stanwich Litigation. We were for some time a defendant in a class action (the “Stanwich Case”) brought in the California Superior Court, Los Angeles County. The original plaintiffs in that case were persons entitled to receive regular payments (the “Settlement Payments”) pursuant to earlier settlements of claims, generally personal injury claims, against unrelated defendants. Stanwich Financial Services Corp. (“Stanwich”), an affiliate of the former chairman of our board of directors, is the entity that was obligated to pay the Settlement Payments. Stanwich defaulted on its payment obligations to the plaintiffs and in June 2001 filed for reorganization under the Bankruptcy Code, in the federal bankruptcy court in Connecticut. By February 2005, we had settled all claims brought against us in the Stanwich Case.

In November 2001, one of the defendants in the Stanwich Case, Jonathan Pardee, asserted claims for indemnity against us in a separate action, which is now pending in federal district court in Rhode Island. We have filed counterclaims in the Rhode Island federal court against Mr. Pardee, and have filed a separate action against Mr. Pardee's Rhode Island attorneys, in the same court. The litigation between Mr. Pardee and us was stayed for several years through September 2011, awaiting resolution of an adversary action brought against Mr. Pardee in the bankruptcy court, which is hearing the bankruptcy of Stanwich.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Pursuant to an agreement with the representative of creditors in the Stanwich bankruptcy, that adversary action has been dismissed. Under that agreement, we paid the bankruptcy estate \$800,000 and abandoned our claims against the estate, while the estate has abandoned its adversary action against Mr. Pardee. With the dismissal of the adversary action, all known claims asserted against Mr. Pardee have been resolved without his incurring any liability. Accordingly, we believe that this resolution of the adversary action will result in limitation of our exposure to Mr. Pardee to no more than some portion of his attorneys fees incurred. The stay in the action against us in Rhode Island has been lifted, and both we and Mr. Pardee filed motions for summary judgment. The court ruled on those motions in February 2013, denying our motion, and granting Mr. Pardee's motion as to liability. The issues remaining for trial are the extent of our obligation to indemnify Mr. Pardee. There is no trial date set, but our expectation is that a trial may be scheduled not earlier than December 2013.

The reader should consider that an adverse judgment against us in the Rhode Island case for indemnification, if in an amount materially in excess of the liability already recorded in respect thereof, could have a material adverse effect on our financial condition or results of operations.

Consumer Litigation. We are routinely involved in various legal proceedings resulting from our consumer finance activities and practices, both continuing and discontinued. We regularly file lawsuits to collect obligations owed to us by consumers, and we are occasionally countersued by such individuals. Consumers can and do initiate lawsuits against us alleging violations of law applicable to collection of receivables, and such lawsuits sometimes allege that resolution as a class action is appropriate. We are currently defending two such class actions. For the most part, we have legal and factual defenses to such claims, which we routinely contest or settle (for immaterial amounts) depending on the particular circumstances of each case. We have recorded a liability as of June 30, 2013 with respect to such matters, in the aggregate.

FTC Action. On July 17, 2013, the staff of the Federal Trade Commission ("FTC") advised us that they are prepared to recommend that the FTC initiate a lawsuit against us relating to allegedly unfair trade practices, and simultaneously advised that settlement of such issues by consent decree may be possible. Based on our review of the FTC's allegations, of past practices of the FTC, of our records of our collection and servicing activities, and of other companies' settlements with the FTC, we expect that we will reach such a settlement, and that such a settlement will require that we make restitutionary payments and that we implement procedural changes under a consent decree. There can be no assurance, however, that we will reach agreement regarding any such settlement, and we may choose to contest the allegations of the FTC. Whether we reach such an agreement or not, the cost to us of contesting or settling the matter may be material. We have recorded a liability as of June 30, 2013 with respect to this matter. The reader should consider that an adverse judgment against us in this matter (whether pursuant to a consent decree or following a contested enforcement action), if in an amount materially in excess of any liability already recorded in respect thereof, could have a material adverse effect on our financial condition or results of operations.

In General. There can be no assurance as to the outcomes of any of the matters referenced above. We have recorded a liability as of June 30, 2013 that we believe represents our best estimate of probable incurred losses for legal contingencies, including the matters referenced above. The amount of losses that are at least reasonably possible above what has already been accrued for cannot be estimated. Any adverse judgment against us, if in an amount materially in excess of the recorded liability, could have a material adverse effect on our financial position or results of operations.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

(10) Employee Benefits

On March 8, 2002 we acquired MFN Financial Corporation and its subsidiaries in a merger. We sponsor the MFN Financial Corporation Benefit Plan (the "Plan"). Plan benefits were frozen June 30, 2001. The table below sets forth the Plan's net periodic benefit cost for the three-month and six-month periods ended June 30, 2013 and 2012.

	Three Months Ended June 30, 2013 2012		Six Months Ended June 30, 2013 2012	
	(In thousands)		(In thousands)	
Components of net periodic cost (benefit)				
Service cost	\$-	\$-	\$-	\$-
Interest Cost	210	220	420	440
Expected return on assets	(335)	(234)	(670)	(468)
Amortization of transition (asset)/obligation	-	-	-	-
Amortization of net (gain) / loss	117	157	234	314
Net periodic cost (benefit)	\$(8)	\$143	\$(16)	\$286

We contributed \$165,000 to the Plan during the three and six-month periods ended June 30, 2013 and we anticipate making contributions in the amount of \$329,000 for the remainder of 2013.

(11) Fair Value Measurements

ASC 820, "Fair Value Measurements" clarifies the principle that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. Under the standard, fair value measurements would be separately disclosed by level within the fair value hierarchy.

ASC 820 defines fair value, establishes a framework for measuring fair value, establishes a three-level valuation hierarchy for disclosure of fair value measurement and enhances disclosure requirements for fair value measurements. The three levels are defined as follows: level 1 - inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets; level 2 – inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument; and level 3 – inputs to the valuation methodology are unobservable and significant to the fair value measurement.

At the time of issuance, five warrants issued between 2008 and 2010 in conjunction with various debt financing transactions contained features that make them subject to derivative accounting. We valued these warrants using a binomial valuation model using a weighted average volatility assumption of 41%, weighted average term of 8 years and a risk free rate of 3.3%. On March 29, 2012 we agreed with the holders to amend three of the five warrants to remove the price reset features that resulted in derivative accounting. On the date of the amendment, we valued each of the three warrants using a binomial pricing model as described above. The aggregate value of the three amended warrants of \$1.1 million was then reclassified from Accounts Payable to Common Stock. On June 25, 2012 we agreed with the holder to amend one other warrant that contained the “down round,” or price reset, features to remove those specific price reset terms. The \$250,000 aggregate value of this amended warrant was reclassified from Accounts Payable to Common Stock on the date of the amendment. The fifth warrant with the “down round” feature was exercised on February 22, 2013. The \$583,000 intrinsic value of this warrant was reclassified from Accounts Payable to Common Stock on the date of the exercise. As of June 30, 2013 all five of the warrants issued that previously contained price reset features have either been amended or exercised and are no longer subject to quarterly valuations.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

In September 2008 we sold automobile contracts in a securitization that was structured as a sale for financial accounting purposes. In that sale, we retained both securities and a residual interest in the transaction that are measured at fair value. In September 2010 we took advantage of improvement in the market for asset-backed securities by re-securitizing the underlying receivables from our unrated September 2008 securitization. We also sold the securities retained from the September 2008 transaction. No gain or loss was recorded as a result of the re-securitization transaction described above. We describe below the valuation methodologies we use for the securities retained and the residual interest in the cash flows of the transaction, as well as the general classification of such instruments pursuant to the valuation hierarchy. The residual interest in such securitization is \$2.2 million as of June 30, 2013 and \$4.8 million as of December 31, 2012 and is classified as level 3 in the three-level valuation hierarchy. We determine the value of that residual interest using a discounted cash flow model that includes estimates for prepayments and losses. We use a discount rate of 20% per annum and a cumulative net loss rate of 14%. The assumptions we use are based on historical performance of automobile contracts we have originated and serviced in the past, adjusted for current market conditions.

In September 2011, we acquired \$217.8 million of finance receivables from Fireside Bank for a purchase price of \$199.6 million. The receivables were acquired by our wholly-owned special purpose subsidiary, CPS Fender Receivables, LLC, which issued a note for \$197.3 million, with a fair value of \$196.5 million. Since the Fireside receivables were originated by another entity with its own underwriting guidelines and procedures, we have elected to account for the Fireside receivables and the related debt secured by those receivables at their estimated fair values so that changes in fair value will be reflected in our results of operations as they occur. Interest income from the receivables and interest expense on the note are included in interest income and interest expense, respectively. Changes to the fair value of the receivables and debt are included in other income. Our level 3, unobservable inputs reflect our own assumptions about the factors that market participants use in pricing similar receivables and debt, and are based on the best information available in the circumstances. They include such inputs as estimated net charge-offs and timing of the amortization of the portfolio of finance receivables. Our estimate of the fair value of the Fireside receivables is performed on a pool basis, rather than separately on each individual receivable. The table below presents a reconciliation of the acquired finance receivables and related debt measured at fair value on a recurring basis using significant unobservable inputs:

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2013	2012	2013	2012
	(in thousands)		(in thousands)	
Finance Receivables Measured at Fair Value:				
Balance at beginning of period	\$43,021	\$126,923	\$59,668	\$160,253
Payments on finance receivables at fair value	(11,461)	(27,607)	(27,980)	(64,103)
Charge-offs on finance receivables at fair value	(739)	(1,547)	(1,740)	(4,050)
Discount accretion	98	1,239	984	5,049

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Mark to fair value	(600)	3,358	(613)	5,217
Balance at end of period	\$30,319	\$102,366	\$30,319	\$102,366

Debt Secured by Finance Receivables Measured at Fair Value:

Balance at beginning of period	\$40,387	\$133,017	\$57,107	\$166,828
Principal payments on debt at fair value	(14,614)	(34,091)	(32,544)	(73,289)
Premium accretion	452	2,126	1,556	5,108
Mark to fair value	(603)	3,610	(497)	6,015
Balance at end of period	25,622	104,662	25,622	104,662
Reduction for principal payments collected and payable	(3,715)	(9,452)	(3,715)	(9,452)
Adjusted balance at end of period	\$21,907	\$95,210	\$21,907	\$95,210

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

The table below compares the fair values of the Fireside receivables and the related secured debt to their contractual balances for the periods shown:

	June 30, 2013		December 31, 2012	
	Contractual Balance	Fair Value	Contractual Balance	Fair Value
Fireside receivables portfolio	\$31,084	\$30,319	\$60,804	\$59,668
Debt secured by Fireside receivables portfolio	8,851	25,622	41,365	57,107

Repossessed vehicle inventory, which is included in Other Assets on our balance sheet, is measured at fair value using level 2 assumptions based on our actual loss experience on sale of repossessed vehicles. At June 30, 2013, the finance receivables related to the repossessed vehicles in inventory totaled \$13.9 million. We have applied a valuation adjustment, or loss allowance, of \$7.6 million, which is based on a recovery rate of 45%, resulting in an estimated fair value and carrying amount of \$6.3 million. The fair value and carrying amount of the repossessed inventory at December 31, 2012 was \$5.7 million after applying a valuation adjustment of \$6.4 million.

There were no transfers in or out of level 1 or level 2 assets and liabilities for the three or six months ended June 30, 2013 and 2012. We have no level 3 assets that are measured at fair value on a non-recurring basis. The table below presents a reconciliation for level 3 assets measured at fair value on a recurring basis using significant unobservable inputs:

	Three Months Ended June 30, 2013		Six Months Ended June 30, 2013	
	2013	2012	2013	2012
Residual Interest in Securitizations:				
Balance at beginning of period	\$3,505	\$4,612	\$4,824	\$4,414
Cash paid (received) during period	(1,259)	4	(2,578)	(22)
Included in earnings	–	234	–	458
Balance at end of period	\$2,246	\$4,850	\$2,246	\$4,850

Warrant Derivative Liability:

Balance at beginning of period	\$-	\$114	\$355	\$967
Included in earnings	-	188	228	391
Reclassification to equity	-	(251)	(583)	(1,307)
Balance at end of period	\$-	\$51	\$-	\$51

20

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

The following table provides certain qualitative information about our level 3 fair value measurements for assets and liabilities carried at fair value:

Financial Instrument	Fair Values as of		Valuation Techniques	Unobservable Inputs	Inputs as of	
	June 30, 2013	December 31, 2012			June 30, 2013	December 31, 2012
Assets:						
Finance receivables measured at fair value	\$30,319	\$59,668	Discounted cash flows	Discount rate	15.4%	20.4%
				Cumulative net losses	4.8%	5.5%
				Monthly average prepayments	0.5%	0.5%
Residual interest in securitizations	2,246	4,824	Discounted cash flows	Discount rate	20.0%	20.0%
				Cumulative net losses	14.0%	13.5%
				Monthly average prepayments	0.5%	0.5%
Liabilities:						
Warrant derivative liability	\$—	\$355	Binomial	Stock price	n/a	\$5.36/sh
				Volatility	n/a	40.0%
				Risk free rate	n/a	1.26%
Debt secured by receivables measured at fair value	25,622	57,107	Discounted cash flows	Discount rate	12.2%	16.2%

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

The estimated fair values of financial assets and liabilities at June 30, 2013 and December 31, 2012, were as follows:

<u>Financial Instrument</u>	As of June 30, 2013 (In thousands)				
	Carrying Value	Fair Value Measurements Using:			Total
		Level 1	Level 2	Level 3	
Assets:					
Cash and cash equivalents	\$ 18,584	\$ 18,584	\$ –	\$–	\$ 18,584
Restricted cash and equivalents	122,864	122,864	–	–	122,864
Finance receivables, net	939,813	–	–	920,878	920,878
Finance receivables measured at fair value	30,319	–	–	30,319	30,319
Residual interest in securitizations	2,246	–	–	2,246	2,246
Accrued interest receivable	12,905	–	–	12,905	12,905
Liabilities:					
Warehouse lines of credit	\$ 17,144	\$–	\$ –	\$ 17,144	\$ 17,144
Accrued interest payable	3,183	–	–	3,183	3,183
Residual interest financing	33,773	–	–	33,773	33,773
Debt secured by receivables measured at fair value	25,622	–	–	25,622	25,622
Securitization trust debt	983,887	–	–	989,285	989,285
Senior secured debt	39,368	–	–	39,368	39,368
Subordinated renewable notes	22,569	–	–	22,569	22,569

<u>Financial Instrument</u>	As of December 31, 2012 (In thousands)				
	Carrying Value	Fair Value Measurements Using:			Total
		Level 1	Level 2	Level 3	
Assets:					
Cash and cash equivalents	\$ 12,966	\$ 12,966	\$ –	\$–	\$ 12,966
Restricted cash and equivalents	104,445	104,445	–	–	104,445
Finance receivables, net	744,749	–	–	740,511	740,511
Finance receivables measured at fair value	59,668	–	–	59,668	59,668
Residual interest in securitizations	4,824	–	–	4,824	4,824
Accrued interest receivable	10,411	–	–	10,411	10,411
Liabilities:					
Warrant derivative liability	\$ 355	\$–	\$ –	\$ 355	\$ 355

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Warehouse lines of credit	21,731	–	–	21,731	21,731
Accrued interest payable	2,795	–	–	2,795	2,795
Residual interest financing	13,773	–	–	13,773	13,773
Debt secured by receivables measured at fair value	57,107	–	–	57,107	57,107
Securitization trust debt	792,497	–	–	803,290	803,290
Senior secured debt	50,135	–	–	50,135	50,135
Subordinated renewable notes	23,281	–	–	23,281	23,281

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The following summary presents a description of the methodologies and assumptions used to estimate the fair value of our financial instruments. Much of the information used to determine fair value is highly subjective. When applicable, readily available market information has been utilized. However, for a significant portion of our financial instruments, active markets do not exist. Therefore, significant elements of judgment were required in estimating fair value for certain items. The subjective factors include, among other things, the estimated timing and amount of cash flows, risk characteristics, credit quality and interest rates, all of which are subject to change. Since the fair value is estimated as of June 30, 2013 and December 31, 2012, the amounts that will actually be realized or paid at settlement or maturity of the instruments could be significantly different.

Cash, Cash Equivalents and Restricted Cash and Equivalents

The carrying value equals fair value.

Finance Receivables, net

The fair value of finance receivables is estimated by discounting future cash flows expected to be collected using current rates at which similar receivables could be originated.

Finance Receivables Measured at Fair Value and Debt Secured by Receivables Measured at Fair Value

The carrying value equals fair value.

Residual Interest in Securitizations

The fair value is estimated by discounting future cash flows using credit and discount rates that we believe reflect the estimated credit, interest rate and prepayment risks associated with similar types of instruments.

Accrued Interest Receivable and Payable

The carrying value approximates fair value because the related interest rates are estimated to reflect current market conditions for similar types of instruments.

Warrant Derivative Liability

The method used to estimate fair value is described above.

Warehouse Lines of Credit, Residual Interest Financing, Senior Secured Debt and Subordinated Renewable Notes

The carrying value approximates fair value because the related interest rates are estimated to reflect current market conditions for similar types of secured instruments.

Securitization Trust Debt

The fair value is estimated by discounting future cash flows using interest rates that we believe reflects the current market rates.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

We are a specialty finance company focused on consumers who have limited credit histories, low incomes or past credit problems, whom we refer to as sub-prime customers. Our business is to purchase and service retail automobile contracts originated primarily by franchised automobile dealers and, to a lesser extent, by select independent dealers in the United States in the sale of new and used automobiles, light trucks and passenger vans. Through our automobile contract purchases, we provide indirect financing to sub-prime customers of dealers. We serve as an alternative source of financing for dealers, facilitating sales to customers who otherwise might not be able to obtain financing from traditional sources, such as commercial banks, credit unions and the captive finance companies affiliated with major automobile manufacturers. In addition to purchasing installment purchase contracts directly from dealers, we have also (i) acquired installment purchase contracts in four merger and acquisition transactions, (ii) purchased immaterial amounts of vehicle purchase money loans from non-affiliated lenders, and (iii) lent money directly to consumers for an immaterial amount of loans secured by vehicles. In this report, we refer to all of such contracts and loans as "automobile contracts."

We were incorporated and began our operations in March 1991. From inception through June 30, 2013, we have purchased a total of approximately \$10.0 billion of automobile contracts from dealers. In addition, we obtained a total of approximately \$842.0 million of automobile contracts in mergers and acquisitions in 2002, 2003, 2004 and 2011. In 2004 and 2009, we were appointed as a third-party servicer for certain portfolios of automobile receivables originated and owned by non-affiliated entities. Beginning in 2008 through the third quarter of 2011, our managed portfolio decreased each year due to our strategy of limiting contract purchases in 2008 and 2009 to conserve our liquidity, as discussed further below. However, since October 2009 we have gradually increased contract purchases, which, in turn has resulted in recent increases to our managed portfolio. Recent contract purchase volumes and managed portfolio levels are shown in the table below:

Period	Contract Purchases and Outstanding Managed Portfolio	
	\$ in thousands	
	Contracts Purchased in Period	Managed Portfolio at Period End
2008	\$296,817	\$1,664,122
2009	8,599	1,194,722
2010	113,023	756,203
2011	284,236	794,649
2012	551,743	897,575
Six months ended June 30, 2013	383,898	1,067,424

We are headquartered in Irvine, California, where most operational and administrative functions are centralized. Credit and underwriting functions are performed in our California headquarters with certain of these functions also performed in our Florida branch. We service our automobile contracts from our California headquarters and our branches in Virginia, Florida and Illinois.

We purchase contracts in our own name (“CPS”) and, until July 2008, also in the name of our wholly-owned subsidiary, TFC. Programs marketed under the CPS name are intended to serve a wide range of sub-prime customers, primarily through franchised new car dealers. Our TFC program served vehicle purchasers enlisted in the U.S. Armed Forces, primarily through independent used car dealers. In July 2008, we suspended contract purchases under our TFC program. We purchase automobile contracts with the intention of financing them on a long-term basis through securitizations. Securitizations are transactions in which we sell a specified pool of contracts to a special purpose entity of ours, which in turn issues asset-backed securities to fund the purchase of the pool of contracts from us.

Securitization and Warehouse Credit Facilities

Throughout the period for which information is presented in this report, we have purchased automobile contracts with the intention of financing them on a long-term basis through securitizations, and on an interim basis through warehouse credit facilities. All such financings have involved identification of specific automobile contracts, sale of those automobile contracts (and associated rights) to one of our special-purpose subsidiaries, and issuance of asset-backed securities or loans to fund the transactions. Depending on the structure, these transactions may properly be accounted for under generally accepted accounting principles as sales of the automobile contracts or as secured financings.

When structured to be treated as a secured financing for accounting purposes, the subsidiary is consolidated with us. Accordingly, the sold automobile contracts and the related debt appear as assets and liabilities, respectively, on our consolidated balance sheet. We then periodically (i) recognize interest and fee income on the contracts, (ii) recognize interest expense on the securities issued in the transaction and (iii) record as expense a provision for credit losses on the contracts.

Since the third quarter of 2003, we have conducted 32 term securitizations. Of these 32, 26 were periodic (generally quarterly) securitizations of automobile contracts that we purchased from automobile dealers under our regular programs. In addition, in March 2004 and November 2005, we completed securitizations of our retained interests in other securitizations that we and our affiliates previously sponsored. The debt from the March 2004 transaction was repaid in August 2005, and the debt from the November 2005 transaction was repaid in May 2007. Also, in June 2004, we completed a securitization of automobile contracts purchased under our TFC program and acquired in a bulk purchase. Further, in December 2005 and May 2007 we completed securitizations that included automobile contracts purchased under the TFC programs, automobile contracts purchased under the CPS programs and automobile contracts we repurchased upon termination of prior securitizations. Since July 2003 all such securitizations have been structured as secured financings, except our September 2008 and September 2010 securitizations. These transactions were in substance sales of the underlying receivables and were treated as sales for financial accounting purposes. The September 2010 securitization was our first securitization since 1993 that did not utilize a financial guaranty for the senior asset-backed notes. Since then we have completed nine senior subordinate securitizations and none have utilized financial guarantees.

Since December 2011, our securitizations have included a pre-funding feature in which a portion of the receivables to be sold to the trust were not delivered until after the initial closing. As a result, our restricted cash balance at June 30, 2013 included \$64.1 million from the proceeds of the sale of the asset-backed notes that were held by the trustee pending delivery of the remaining receivables. In July 2013, the requisite additional receivables were delivered to the trust and we received the related restricted cash, a portion of which was used to repay amounts owed under our warehouse credit facilities.

Portfolio Acquisitions

As stated above, we have acquired approximately \$822.8 million in finance receivables through four acquisitions. These transactions took place in 2002, 2003, 2004 and September 2011. The September 2011 acquisition consisted of approximately \$217.8 million of finance receivables that we purchased from Fireside Bank of Pleasanton, California.

Uncertainty of Capital Markets and General Economic Conditions

We depend upon the availability of warehouse credit facilities and access to long-term financing through the issuance of asset-backed securities collateralized by our automobile contracts. Since 1994, we have completed 59 term securitizations of approximately \$8.1 billion in contracts. From the fourth quarter of 2007 through the end of 2009, we observed unprecedented adverse changes in the market for securitized pools of automobile contracts. These changes included reduced liquidity, and reduced demand for asset-backed securities, particularly for securities carrying a financial guaranty and for securities backed by sub-prime automobile receivables. Moreover, during that period many of the firms that previously provided financial guarantees, which were an integral part of our securitizations, suspended offering such guarantees. These adverse changes caused us to conserve liquidity by significantly reducing our purchases of automobile contracts. However, since October 2009 we have established new funding facilities and gradually increased our contract purchases and the frequency and amount of our term securitizations. Our recent history of term securitizations is summarized in the table below:

Recent Asset-Backed Term Securitizations

Period	<i>\$ in thousands</i>	
	Number of Term Securitizations	Amount of Term Securitizations
2006	4	\$ 957.7
2007	3	1,118.1
2008	2	509.0
2009	0	–
2010	1	103.8
2011	3	335.6
2012	4	603.5
Six months ended June 30, 2013	2	390.0

Our 2012 securitizations included \$58.2 million in contracts that were repurchased in 2012 from securitizations closed in 2006 and 2007. Our 2013 securitizations included \$7.4 million in contracts that were repurchased from a securitization closed in 2008. Since 2011 all of our securitizations have been structured as secured financings and none utilized financial guarantees.

Our current short-term funding capacity is \$200 million, comprising two credit facilities. The first \$100 million credit facility was established in December 2010. This facility was renewed in March 2013, extending the revolving period to March 2015, and adding an amortization period through March 2017. Our second \$100 million credit facility was established in May 2012. This facility was renewed in June 2013, extending the revolving period to June 2015, and adding an amortization period through June 2016.

Financial Covenants

Certain of our securitization transactions, our warehouse credit facilities and our residual interest financing contain various financial covenants requiring certain minimum financial ratios and results. Such covenants include maintaining minimum levels of liquidity and net worth and not exceeding maximum leverage levels. As of June 30, 2013 we were in compliance with all such covenants. In addition, certain securitization and non-securitization related debt contain cross-default provisions that would allow certain creditors to declare a default if a default occurred under a different facility.

Results of Operations

Comparison of Operating Results for the three months ended June 30, 2013 with the three months ended June 30, 2012

Revenues. In April 2013, we repurchased the outstanding Class D notes from our first 2008 securitization for a cash payment and a new note. We subsequently exercised our “clean-up call” option and repurchased the remaining collateral from the related securitization trust. The aggregate value of our consideration for the Class D notes was \$10.9 million less than our carrying value of the Class D notes at the time of the repurchase. As a result of the repurchase of the Class D notes and the termination of the securitization trust, we realized a gain of \$10.9 million, or 15.5% of our total revenues of \$70.5 million for the three months ended June 30, 2013.

During the three months ended June 30, 2013, excluding the gain on cancellation of debt of \$10.9 million, our revenues were \$59.5 million, an increase of \$15.3 million, or 34.8%, from the prior year revenue of \$44.2 million. The primary reason for the increase in revenues is an increase in interest income. Interest income for the three months ended June 30, 2013 increased \$14.3 million, or 34.3%, to \$55.8 million from \$41.5 million in the prior year. The primary reason for the increase in interest income is the increase in finance receivables held by consolidated subsidiaries, which increased from \$721.6 million at June 30, 2012 to \$948.0 million at June 30, 2013. The table below shows the average balances of our portfolio held by consolidated subsidiaries for the three months ended June 30, 2013 and 2012:

	Average Balances for the	
	Three Months Ended	
	June 30, 2013	June 30, 2012
	Amount	Amount
Finance Receivables Owned by Consolidated Subsidiaries	(\$ in millions)	
CPS Originated Receivables	\$983.4	\$630.2
Fireside	34.7	113.3
Total	\$1,018.1	\$743.5

Servicing fees totaling \$876,000 in the three months ended June 30, 2013 increased \$281,000, or 47.3%, from \$595,000 in the prior year. We earn base servicing fees on two portfolios that are decreasing in size as we receive customer payments and, consequently, base servicing fees are decreasing also. On one of those portfolios, however, we recently began earning an incentive servicing fee. Such incentive servicing fee was \$521,000 for the three months ended June 30, 2013 and more than offset the decrease of \$240,000 in base servicing fees. We did not earn any incentive servicing fee in the prior year's period. As of June 30, 2013 and 2012, our managed portfolio owned by consolidated vs. non-consolidated subsidiaries and other third parties was as follows:

	June 30, 2013		June 30, 2012	
	Amount (1)	% (2)	Amount (1)	% (2)
Total Managed Portfolio	(\$ in millions)			
Owned by Consolidated Subsidiaries				
CPS Originated Receivables	\$1,021.7	95.7%	\$654.2	81.2%
Fireside	31.1	2.9%	104.0	12.9%
Owned by Non-Consolidated Subsidiaries	8.8	0.8%	27.9	3.5%
Third-Party Servicing Portfolios	5.8	0.5%	20.0	2.5%
Total	\$1,067.4	100.0%	\$806.1	100.0%

(1) Contractual balances.

(2) Percentages may not add up to 100% due to rounding.

At June 30, 2013, we were generating income and fees on a managed portfolio with an outstanding principal balance of \$1,067.4 million (this amount includes \$8.8 million of automobile contracts on which we earn servicing fees and own a residual interest and also includes another \$5.8 million of automobile contracts on which we earn base and incentive servicing fees), compared to a managed portfolio with an outstanding principal balance of \$806.1 million as of June 30, 2012. At June 30, 2013 and 2012, the managed portfolio composition was as follows:

Originating Entity	June 30, 2013		June 30, 2012	
	Amount (1)	% (2)	Amount (1)	% (2)
	(\$ in millions)			
CPS	\$1,030.5	96.5%	\$681.5	84.5%
Fireside	31.1	2.9%	104.0	12.9%
TFC	–	0.0%	0.6	0.1%
Third Party Portfolio	5.8	0.5%	20.0	2.5%
Total	\$1,067.4	100.0%	\$806.1	100.0%

(1) Contractual balances.

(2) Percentages may not add up to 100% due to rounding.

Other income increased by \$852,000, or 42.4%, to \$2.9 million in the three months ended June 30, 2013 from \$2.0 million during the prior year. The increase is comprised of a net increase of \$255,000 in the fair value of the receivables and debt associated with the Fireside portfolio acquisition, an increase of \$731,000 from fees associated with direct mail and other related products and services that we offer to our dealers, and an increase of \$138,000 in payments from third-party providers of convenience fees paid by our customers for web based and other electronic payments. These increases were partially offset by decreases in sales tax refunds of \$55,000, and a decrease of \$94,000 in recoveries on receivables from the 2002 acquisition of MFN Financial Corporation.

Expenses. Our operating expenses consist largely of provision for credit losses, interest expense, employee costs and general and administrative expenses. Provision for credit losses and interest expense are significantly affected by the volume of automobile contracts we purchased during the trailing 12-month period and by the outstanding balance of finance receivables held by consolidated subsidiaries. Employee costs and general and administrative expenses are incurred as applications and automobile contracts are received, processed and serviced. Factors that affect margins and net income include changes in the automobile and automobile finance market environments, and macroeconomic factors such as interest rates and changes in the unemployment level.

Employee costs include base salaries, commissions and bonuses paid to employees, and certain expenses related to the accounting treatment of outstanding stock options, and are one of our most significant operating expenses. These costs (other than those relating to stock options) generally fluctuate with the level of applications and automobile contracts processed and serviced.

Other operating expenses consist largely of facilities expenses, telephone and other communication services, credit services, computer services, marketing and advertising expenses, and depreciation and amortization.

During the three months ended June 30, 2013, we recognized \$9.7 million in contingent liability expenses to either record or increase the amounts we believe we may incur related to various pending litigation. The amount was allocated in part to a long running case we refer to as the Stanwich litigation, and also to more recent matters including two California class action suits where we are the defendant, and a governmental inquiry, in which the United States Federal Trade Commission ("FTC") has informally proposed that we refrain from certain allegedly unfair trade practices, and make restitutionary payments into a consumer relief fund.

The following comparison of our expenses for the three months ended June 30, 2013 and 2012 excludes the impact of the \$9.7 million contingent liability expense incurred in the three months ended June 30, 2013.

Total operating expenses, excluding the \$9.7 million in contingent liability expense, were \$52.3 million for the three months ended June 30, 2013, compared to \$42.8 million for the prior year, an increase of \$9.5 million, or 22.1%. The increase is primarily due to the increase in the amount of new contracts we purchased, the resulting increase in our consolidated portfolio and associated servicing costs, and the related increase in our provision for credit losses. Increases in provision for credit losses were somewhat offset by decreases in interest expense.

Employee costs increased by \$3.3 million or 39.3%, to \$11.5 million during the three months ended June 30, 2013, representing 22.0% of total operating expenses, from \$8.3 million for the prior year, or 19.3% of total operating expenses. Since 2010, we have added employees in our Originations and Marketing departments to accommodate the increase in contract purchases. These additions have offset reductions in our Servicing department staff that have resulted from decreases in the number of accounts in our managed portfolio. The table below summarizes our employees by category as well as contract purchases and units in our managed portfolio as of, and for the three-month periods, ended June 30, 2013 and 2012:

	June 30, 2013	June 30, 2012
	Amount	Amount
	(\$ in millions)	
Contracts purchased (dollars)	\$203.8	\$137.9
Contracts purchased (units)	12,819	8,871
Managed portfolio outstanding (dollars)	\$1,067.4	\$806.1
Managed portfolio outstanding (units)	93,332	96,024
Number of Originations staff	151	107
Number of Marketing staff	100	71
Number of Servicing staff	295	300
Number of other staff	67	60
Total number of employees	613	538

General and administrative expenses include costs associated with purchasing and servicing our portfolio of finance receivables, including expenses for facilities, credit services, and telecommunications. General and administrative expenses were \$4.5 million, an increase of \$941,000, or 26.3%, compared to the previous year and represented 8.6% of total operating expenses.

Interest expense for the three months ended June 30, 2013 decreased by \$5.2 million to \$14.6 million, or 26.4%, compared to \$19.8 million in the previous year. Interest expense on the Fireside portfolio credit facility decreased by \$3.3 million compared to the prior period as the Fireside portfolio and the related debt have paid down to significantly lower levels over the last year.

Interest on securitization trust debt decreased by \$909,000 for the three months ended June 30, 2013 compared to the prior year. Although the outstanding amount of securitization trust debt increased to \$983.9 million at June 30, 2013 compared to \$666.1 million at June 30, 2012, the blended interest rates on our term securitizations since 2012 are significantly less than the blended interest rates on securitization trust debt incurred prior to 2012.

Interest expense on senior secured and subordinated debt decreased by \$1.1 million, due primarily to our repayment, in April 2013 of \$15.0 million in senior secured debt and also to a reduction in the interest rate on the remaining senior secured debt. Interest expense on residual interest financing increased \$448,000 in the three months ended June 30, 2013 compared to the prior year. The increase is due to the addition, in April 2013 of a new \$20 million residual interest financing.

Interest expense on warehouse debt decreased by \$371,000 for the three months ended June 30, 2013 compared to the prior year. Although we increased our contract purchases to \$203.8 million for the three months ended June 30, 2013 compared to \$137.9 million in the prior period, recently we have relied less on warehouse credit facilities and instead have used more of our unrestricted cash balances to hold receivables prior to securitization.

Provision for credit losses was \$17.4 million for the three months ended June 30, 2013, an increase of \$9.7 million, or 125.3% compared to the prior year and represented 33.2% of total operating expenses. The provision for credit losses maintains the allowance for finance credit losses at levels that we feel are adequate for probable incurred credit losses that can be reasonably estimated. Our approach for establishing the allowance requires greater amounts of provision for credit losses early in the terms of our finance receivables. Consequently, the increase in provision expense is the result of the increase in our contract purchases during the last year and the increased size of the portfolio owned by our consolidated subsidiaries compared to the prior year.

Marketing expenses consist primarily of commission-based compensation paid to our employee marketing representatives. Our marketing representatives earn a salary plus commissions based on volume of contract purchases and sales of ancillary products and services that we offer our dealers, such as training programs, internet lead sales, and direct mail products. Marketing expenses increased by \$912,000, or 35.6%, to \$3.5 million during the three months ended June 30, 2013, compared to \$2.6 million in the prior year period, and represented 6.6% of total operating expenses. For the three months ended June 30, 2013, we purchased 12,819 contracts representing \$203.8 million in receivables in the current period compared to 8,871 contracts representing \$137.9 million in receivables in the prior year.

Occupancy expenses decreased by \$43,000 or 5.9%, to \$683,000 compared to \$726,000 in the previous year and represented 1.3% of total operating expenses.

Depreciation and amortization expenses decreased by \$18,000 or 13.6%, to \$114,000 compared to \$132,000 in the previous year and represented 0.2% of total operating expenses.

For the three months ended June 30, 2013, we recorded income tax expense of \$3.7 million. In the prior year period, we recorded no income tax expense but we reduced our valuation allowance for our deferred tax assets by \$400,000.

Comparison of Operating Results for the six months ended June 30, 2013 with the six months ended June 30, 2012

Revenues. In April 2013, we repurchased the outstanding Class D notes from our first 2008 securitization for a cash payment and a new note. We subsequently exercised our “clean-up call” option and repurchased the remaining collateral from the related securitization trust. The aggregate value of our consideration for the Class D notes was \$10.9 million less than our carrying value of the Class D notes at the time of the repurchase. As a result of the repurchase of the Class D notes and the termination of the securitization trust, we realized a gain of \$10.9 million, or 8.8% of our total revenues of \$125.1 million for the six months ended June 30, 2013.

During the six months ended June 30, 2013, excluding the gain on cancellation of debt of \$10.9 million, our revenues were \$114.1 million, an increase of \$25.5 million, or 28.7%, from the prior year revenue of \$88.7 million. The primary reason for the increase in revenues is an increase in interest income. Interest income for the six months ended June 30, 2013 increased \$24.8 million, or 30.2%, to \$107.0 million from \$82.2 million in the prior year. The primary reason for the increase in interest income is the increase in finance receivables held by consolidated subsidiaries, which increased from \$721.6 million at June 30, 2012 to \$948.0 million at June 30, 2013. The table below shows the average balances of our portfolio held by consolidated subsidiaries for the six months ended June 30, 2013 and 2012:

	Average Balances for the	
	Six Months Ended	
	June 30, 2013	June 30, 2012
	Amount	Amount
Finance Receivables Owned by Consolidated Subsidiaries	(\$ in millions)	
CPS Originated Receivables	\$927.6	\$ 600.6
Fireside	41.9	129.9
Total	\$969.5	\$ 730.5

Servicing fees totaling \$1.8 million for the six months ended June 30, 2013 increased \$388,000, or 27.8%, from \$1.4 million in the prior year. We earn base servicing fees on two portfolios that are decreasing in size as we receive customer payments and, consequently, base servicing fees are decreasing also. On one of those portfolios, however, we recently began earning an incentive servicing fee. Such incentive servicing fee was \$986,000 for the six months ended June 30, 2013 and more than offset the decrease of \$598,000 in base servicing fees. We did not earn any incentive servicing fee in the prior year's period. As of June 30, 2013 and 2012, our managed portfolio owned by consolidated vs. non-consolidated subsidiaries and other third parties was as follows:

	June 30, 2013		June 30, 2012	
	Amount (1)	% (2)	Amount (1)	% (2)
Total Managed Portfolio	(\$ in millions)			
Owned by Consolidated Subsidiaries				
CPS Originated Receivables	\$ 1,021.7	95.7%	\$ 654.2	81.2%
Fireside	31.1	2.9%	104.0	12.9%
Owned by Non-Consolidated Subsidiaries	8.8	0.8%	27.9	3.5%
Third-Party Servicing Portfolios	5.8	0.5%	20.0	2.5%
Total	\$ 1,067.4	100.0%	\$ 806.1	100.0%

(1) Contractual balances.

(2) Percentages may not add up to 100% due to rounding.

At June 30, 2013, we were generating income and fees on a managed portfolio with an outstanding principal balance of \$1,067.4 million (this amount includes \$8.8 million of automobile contracts on which we earn servicing fees and own a residual interest and also includes another \$5.8 million of automobile contracts on which we earn base and incentive servicing fees), compared to a managed portfolio with an outstanding principal balance of \$806.1 million as of June 30, 2012. At June 30, 2013 and 2012, the managed portfolio composition was as follows:

	June 30, 2013		June 30, 2012	
	Amount (1)	% (2)	Amount (1)	% (2)
Originating Entity	(\$ in millions)			
CPS	\$ 1,030.5	96.5%	\$ 681.5	84.5%
Fireside	31.1	2.9%	104.0	12.9%
TFC	–	0.0%	0.6	0.1%
Third Party Portfolio	5.8	0.5%	20.0	2.5%
Total	\$ 1,067.4	100.0%	\$ 806.1	100.0%

(1) Contractual balances.

(2) Percentages may not add up to 100% due to rounding.

Other income increased by \$264,000, or 5.2%, to \$5.4 million in the six months ended June 30, 2013 from \$5.1 million during the prior year. The increase includes an increase of \$697,000 from fees associated with direct mail and other related products and services that we offer to our dealers. This increase was partially offset by decreases of \$214,000 in the fair value of receivables and debt associated with the Fireside portfolio acquisition, decreases in sales tax refunds of \$43,000, and a decrease of \$177,000 in recoveries on receivables from the 2002 acquisition of MFN Financial Corporation.

Expenses. Our operating expenses consist largely of provision for credit losses, interest expense, employee costs and general and administrative expenses. Provision for credit losses and interest expense are significantly affected by the volume of automobile contracts we purchased during the trailing 12-month period and by the outstanding balance of finance receivables held by consolidated subsidiaries. Employee costs and general and administrative expenses are incurred as applications and automobile contracts are received, processed and serviced. Factors that affect margins and net income include changes in the automobile and automobile finance market environments, and macroeconomic factors such as interest rates and changes in the unemployment level.

Employee costs include base salaries, commissions and bonuses paid to employees, and certain expenses related to the accounting treatment of outstanding stock options, and are one of our most significant operating expenses. These costs (other than those relating to stock options) generally fluctuate with the level of applications and automobile contracts processed and serviced.

Other operating expenses consist largely of facilities expenses, telephone and other communication services, credit services, computer services, marketing and advertising expenses, and depreciation and amortization.

During the six months ended June 30, 2013, we recognized \$9.7 million in contingent liability expenses to either record or increase the amounts we believe we may incur related to various pending litigation. The amount was allocated in part to a long running case we refer to as the Stanwich litigation, and also to more recent matters including two California class action suits where we are the defendant, and a governmental inquiry, in which the United States Federal Trade Commission ("FTC") has informally proposed that we refrain from certain allegedly unfair trade practices, and make restitutionary payments into a consumer relief fund.

The following comparison of our expenses for the six months ended June 30, 2013 and 2012 excludes the impact of the \$9.7 million contingent liability expense incurred in the six months ended June 30, 2013.

Total operating expenses, excluding the \$9.7 million in contingent liability expense, were \$100.4 million for the six months ended June 30, 2013, compared to \$86.8 million for the prior year, an increase of \$13.5 million, or 15.6%. The increase is primarily due to the increase in the amount of new contracts we purchased, the resulting increase in our

consolidated portfolio and associated servicing costs, and the related increase in our provision for credit losses. Increases in provision for credit losses were somewhat offset by decreases in interest expense.

Employee costs increased by \$3.3 million or 19.4%, to \$20.5 million for the six months ended June 30, 2013, representing 20.4% of total operating expenses, from \$17.1 million for the prior year, or 19.8% of total operating expenses. Since 2010, we have added employees in our Originations and Marketing departments to accommodate the increase in contract purchases. These additions have offset reductions in our Servicing department staff that have resulted from decreases in the number of accounts in our managed portfolio. The table below summarizes our employees by category as well as contract purchases and units in our managed portfolio as of, and for the six-month periods, ended June 30, 2013 and 2012:

	June 30, 2013	June 30, 2012
	Amount	Amount
	(\$ in millions)	
Contracts purchased (dollars)	\$383.9	\$257.8
Contracts purchased (units)	24,510	16,813
Managed portfolio outstanding (dollars)	\$1,067.4	\$806.1
Managed portfolio outstanding (units)	93,332	96,024
Number of Originations staff	151	107
Number of Marketing staff	100	71
Number of Servicing staff	295	300
Number of other staff	67	60
Total number of employees	613	538

General and administrative expenses include costs associated with purchasing and servicing our portfolio of finance receivables, including expenses for facilities, credit services, and telecommunications. General and administrative expenses were \$8.3 million, an increase of \$197,000, or 2.4%, compared to the previous year and represented 8.2% of total operating expenses.

Interest expense for the six months ended June 30, 2013 decreased by \$11.2 million to \$30.9 million, or 26.6%, compared to \$42.1 million in the previous year. Interest expense on the Fireside portfolio credit facility decreased by \$7.3 million compared to the prior period as the Fireside portfolio and the related debt have paid down to significantly lower levels over the last year.

Interest on securitization trust debt decreased by \$1.8 million in the six months ended June 30, 2013 compared to the prior year. Although the outstanding amount of securitization trust debt increased to \$983.9 million at June 30, 2013 compared to \$666.1 million at June 30, 2012, the blended interest rates on our term securitizations since 2012 are significantly less than the blended interest rates on securitization trust debt incurred prior to 2012.

Interest expense on senior secured and subordinated debt decreased by \$1.8 million, due primarily to our repayment, in April 2013 of \$15.0 million in senior secured debt and also to a reduction in the interest rate on the remaining senior secured debt. Interest expense on residual interest financing increased \$192,000 in the six months ended June 30, 2013 compared to the prior year. The increase is due to the addition, in April 2013 of a new \$20 million residual interest financing.

Interest expense on warehouse debt decreased by \$485,000 for the six months ended June 30, 2013 compared to the prior year. Although we increased our contract purchases to \$383.9 million for the six months ended June 30, 2013 compared to \$257.8 million in the prior period, recently we have relied less on warehouse credit facilities and instead

have used more of our unrestricted cash balances to hold receivables prior to securitization.

Provision for credit losses was \$32.5 million for the six months ended June 30, 2013, an increase of \$20.0 million, or 159.2%, compared to the prior year and represented 32.4% of total operating expenses. The provision for credit losses maintains the allowance for finance credit losses at levels that we feel are adequate for probable incurred credit losses that can be reasonably estimated. Our approach for establishing the allowance requires greater amounts of provision for credit losses early in the terms of our finance receivables. Consequently, the increase in provision expense is the result of the increase in our contract purchases during the last year and the increased size of the portfolio owned by our consolidated subsidiaries compared to the prior year.

Marketing expenses consist primarily of commission-based compensation paid to our employee marketing representatives. Our marketing representatives earn a salary plus commissions based on volume of contract purchases and sales of ancillary products and services that we offer our dealers, such as training programs, internet lead sales, and direct mail products. Marketing expenses increased by \$1.5 million, or 28.5%, to \$6.7 million during the six months ended June 30, 2013, compared to \$5.2 million in the prior year period, and represented 6.6% of total operating expenses. For the six months ended June 30, 2013, we purchased 24,510 contracts representing \$383.9 million in receivables in the current period compared to 16,813 contracts representing \$257.8 million in receivables in the prior year.

Occupancy expenses decreased by \$221,000 or 15.3%, to \$1.2 million compared to \$1.4 million in the previous year and represented 1.2% of total operating expenses.

Depreciation and amortization expenses decreased by \$27,000, or 9.5%, to \$257,000 compared to \$284,000 in the previous year and represented 0.3% of total operating expenses.

For the six months ended June 30, 2013, we recorded income tax expense of \$6.5 million. In the prior year period, we recorded no income tax expense but we reduced our valuation allowance for our deferred tax assets by \$700,000.

Credit Experience

Our financial results are dependent on the performance of the automobile contracts in which we retain an ownership interest. Broad economic factors such as recession and significant changes in unemployment levels influence the credit performance of our portfolio, as does the weighted average age of the receivables at any given time. The tables below document the delinquency, repossession and net credit loss experience of all such automobile contracts that we were servicing and owned as of the respective dates shown. The tables do not include the experience of third party servicing portfolios.

Delinquency Experience (1)

Total Owned Portfolio Excluding Fireside

	June 30, 2013		June 30, 2012		December 31, 2012	
	Number of Contracts	Amount	Number of Contracts	Amount	Number of Contracts	Amount
	(Dollars in thousands)					
Delinquency Experience						
Gross servicing portfolio (1)	83,253	\$ 1,030,498	69,916	\$ 682,110	74,124	\$ 825,186
Period of delinquency (2)						
31-60 days	2,442	\$ 21,513	1,790	\$ 10,553	2,545	\$ 18,034
61-90 days	1,319	11,637	771	4,625	1,179	9,360
91+ days	665	5,502	404	2,486	773	5,297
Total delinquencies (2)	4,426	38,652	2,965	17,664	4,497	32,691
Amount in repossession (3)	1,661	14,036	1,633	8,449	1,932	12,506

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Total delinquencies and amount in repossession (2)	6,087	\$52,688	4,598	\$26,113	6,429	\$45,197
Delinquencies as a percentage of gross servicing portfolio	5.3%	3.8%	4.2%	2.6%	6.1%	4.0%
Total delinquencies and amount in repossession as a percentage of gross servicing portfolio	7.3%	5.1%	6.6%	3.8%	8.7%	5.5%
Extension Experience						
Contracts with one extension, accruing	10,165	\$109,453	10,100	\$61,208	9,094	\$73,632
Contracts with two or more extensions, accruing	5,998	30,688	10,077	53,805	7,795	37,761
	16,163	140,141	20,177	115,013	16,889	111,393
Contracts with one extension, non-accrual	530	5,228	464	2,191	632	4,401
Contracts with two or more extensions, non-accrual	561	2,366	780	3,944	1,044	4,344
	1,091	7,594	1,244	6,135	1,676	8,745
Total contracts with extensions	17,254	\$147,735	21,421	\$121,148	18,565	\$120,138

Delinquency Experience (1)

Fireside Portfolio

	June 30, 2013		June 30, 2012		December 31, 2012	
	Number of Contracts	Amount	Number of Contracts	Amount	Number of Contracts	Amount
<i>Delinquency Experience</i>						
Gross servicing portfolio (1)	8,724	\$ 31,084	22,594	\$ 104,033	15,039	\$ 60,807
Period of delinquency (2)						
31-60 days	400	\$ 1,309	496	\$ 1,878	621	\$ 2,206
61-90 days	133	399	231	872	204	710
91+ days	64	148	84	339	114	331
Total delinquencies (2)	597	1,856	811	3,089	939	3,247
Amount in repossession (3)	55	236	146	714	175	703
Total delinquencies and amount in repossession (2)	652	\$ 2,092	957	\$ 3,803	1,114	\$ 3,950
Delinquencies as a percentage of gross servicing portfolio	6.8%	6.0%	3.6%	3.0%	6.2%	5.3%
Total delinquencies and amount in repossession as a percentage of gross servicing portfolio	7.5%	6.7%	4.2%	3.7%	7.4%	6.5%
Extension Experience						
Contracts with one extension, accruing	2,210	\$ 9,116	2,589	\$ 14,887	3,117	\$ 15,262
Contracts with two or more extensions, accruing	526	2,561	18	282	134	717
	2,736	11,677	2,607	15,169	3,251	15,979
Contracts with one extension, non-accrual	50	185	53	282	160	726
Contracts with two or more extensions, non-accrual	8	33	1	6	6	20
	58	218	54	288	166	746
Total contracts with extensions	2,794	\$ 11,895	2,661	\$ 15,457	3,417	\$ 16,725

Delinquency Experience (1)

Total Owned Portfolio

	June 30, 2013		June 30, 2012		December 31, 2012	
	Number of Contracts	Amount	Number of Contracts	Amount	Number of Contracts	Amount
	(Dollars in thousands)					
Delinquency Experience						
Gross servicing portfolio (1)	91,977	\$1,061,582	92,510	\$786,144	89,163	\$885,993
Period of delinquency (2)						
31-60 days	2,842	\$22,822	2,286	\$12,431	3,166	\$20,240
61-90 days	1,452	12,036	1,002	5,497	1,383	10,070
91+ days	729	5,649	488	2,825	887	5,629
Total delinquencies (2)	5,023	40,507	3,776	20,753	5,436	35,939
Amount in repossession (3)	1,716	14,272	1,779	9,164	2,107	13,209
Total delinquencies and amount in repossession (2)	6,739	\$54,779	5,555	\$29,917	7,543	\$49,148
Delinquencies as a percentage of gross servicing portfolio	5.5%	3.8%	4.1%	2.6%	6.1%	4.1%
Total delinquencies and amount in repossession as a percentage of gross servicing portfolio	7.3%	5.2%	6.0%	3.8%	8.5%	5.5%
Extension Experience						
Contracts with one extension, accruing	12,375	\$118,569	12,689	\$76,095	12,211	\$88,894
Contracts with two or more extensions, accruing	6,524	33,219	10,095	53,887	7,929	38,478
	18,899	151,788	22,784	129,982	20,140	127,372
Contracts with one extension, non-accrual	580	5,413	517	2,473	792	5,127
Contracts with two or more extensions, non-accrual	569	2,399	781	3,947	1,050	4,364
	1,149	7,812	1,298	6,420	1,842	9,491
	20,048	\$159,600	24,082	\$136,402	21,982	\$136,863

(1) All amounts and percentages are based on the amount remaining to be repaid on each automobile contract, including, for pre-computed automobile contracts, any unearned interest. The information in the table represents the gross principal amount of all automobile contracts we have purchased, including automobile contracts subsequently sold to or financed in securitization transactions that we continue to service.

(2) We consider an automobile contract delinquent when an obligor fails to make at least 90% of a contractually due payment by the following due date, which date may have been extended within limits specified in the Servicing Agreements. The period of delinquency is based on the number of days payments are contractually past due, as

extended where applicable. Automobile contracts less than 31 days delinquent are not included.

(3) Amount in repossession represents financed vehicles that have been repossessed but not yet liquidated.

Net Charge-Off Experience (1)

Total Owned Portfolio Excluding Fireside

**June
30,**