

CREDIT ACCEPTANCE CORP  
Form 10-Q  
November 01, 2012

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

(Mark One)

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

For the quarterly period ended September 30, 2012

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

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

MICHIGAN  
(State or other jurisdiction of incorporation or  
organization)

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

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

48034-8339  
(Zip Code)

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

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

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

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

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

Large accelerated  
filer

Accelerated filer

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

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

The number of shares of Common Stock, par value \$0.01, outstanding on October 19, 2012 was 24,551,189.

---

TABLE OF CONTENTS

PART I. — FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

Consolidated Balance Sheets – As of September 30, 2012 and December 31, 2011 1

Consolidated Statements of Income – Three and nine months ended September 30, 2012 and 2011 2

Consolidated Statements of Comprehensive Income – Three and nine months ended September 30, 2012 and 2011 3

Consolidated Statements of Cash Flows – Nine months ended September 30, 2012 and 2011 4

Notes to Consolidated Financial Statements 5

ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS 32

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK 45

ITEM 4. CONTROLS AND PROCEDURES 45

PART II. — OTHER INFORMATION

ITEM 1A. RISK FACTORS 46

ITEM 6. EXHIBITS 46

SIGNATURE 47

Table of Contents

## PART I. - FINANCIAL INFORMATION

## ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

CREDIT ACCEPTANCE CORPORATION  
CONSOLIDATED BALANCE SHEETS

(In thousands, except per share data)

	As of	
	September 30, 2012 (Unaudited)	December 31, 2011
<b>ASSETS:</b>		
Cash and cash equivalents	\$ 5,725	\$ 4,657
Restricted cash and cash equivalents	167,706	104,679
Restricted securities available for sale	–	810
Loans receivable (including \$5,634 and \$4,949 from affiliates as of September 30, 2012 and December 31, 2011, respectively)	2,047,481	1,752,891
Allowance for credit losses	(170,763)	(154,318)
Loans receivable, net	1,876,718	1,598,573
Property and equipment, net	21,863	18,472
Income taxes receivable	–	506
Other assets	31,310	30,901
Total Assets	\$ 2,103,322	\$ 1,758,598
<b>LIABILITIES AND SHAREHOLDERS' EQUITY:</b>		
<b>Liabilities:</b>		
Accounts payable and accrued liabilities	\$ 98,131	\$ 95,858
Revolving secured line of credit	115,800	43,900
Secured financing	791,850	599,281
Mortgage note	4,104	4,288
Senior notes	350,307	350,378
Deferred income taxes, net	135,334	123,449
Income taxes payable	9,991	1,493
Total Liabilities	1,505,517	1,218,647
Commitments and Contingencies - See Note 13		
<b>Shareholders' Equity:</b>		
Preferred stock, \$.01 par value, 1,000 shares authorized, none issued	–	–
	246	256

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

Common stock, \$.01 par value, 80,000 shares authorized, 24,551 and 25,624 shares issued and outstanding as of September 30, 2012 and December 31, 2011, respectively		
Paid-in capital	49,455	38,801
Retained earnings	548,104	500,888
Accumulated other comprehensive income	–	6
Total Shareholders' Equity	597,805	539,951
Total Liabilities and Shareholders' Equity	\$ 2,103,322	\$ 1,758,598

See accompanying notes to consolidated financial statements.

Table of Contents

CREDIT ACCEPTANCE CORPORATION  
CONSOLIDATED STATEMENTS OF INCOME  
(UNAUDITED)

(In thousands, except per share data)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2012	2011	2012	2011
Revenue:				
Finance charges	\$137,495	\$117,905	\$397,563	\$338,238
Premiums earned	12,206	10,462	34,987	29,195
Other income	5,977	5,372	17,313	19,783
Total revenue	155,678	133,739	449,863	387,216
Costs and expenses:				
Salaries and wages	21,720	15,929	61,530	47,402
General and administrative	6,797	6,044	21,463	18,186
Sales and marketing	8,129	5,587	23,478	17,768
Provision for credit losses	9,759	4,550	17,716	22,394
Interest	16,289	14,600	47,150	42,173
Provision for claims	9,122	8,363	26,704	22,733
Total costs and expenses	71,816	55,073	198,041	170,656
Income before provision for income taxes	83,862	78,666	251,822	216,560
Provision for income taxes	30,874	28,706	91,983	78,565
Net income	\$52,988	\$49,960	159,839	137,995
Net income per share:				
Basic	\$2.13	\$1.92	\$6.24	\$5.23
Diluted	\$2.12	\$1.91	\$6.22	\$5.19
Weighted average shares outstanding:				
Basic	24,908	26,033	25,629	26,397
Diluted	24,962	26,136	25,706	26,573

See accompanying notes to consolidated financial statements.



Table of Contents

CREDIT ACCEPTANCE CORPORATION  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
(UNAUDITED)

(In thousands)	For the Three Months Ended September 30,	
	2012	2011
Net income	\$ 52,988	\$ 49,960
Other comprehensive income, net of tax:		
Unrealized loss on derivatives qualifying as hedges		
Unrealized loss on cash flow hedge, net of tax of \$0 and \$0 for 2012 and 2011, respectively	-	-
Less: reclassification adjustment for loss on cash flow hedge included in net income, net of tax of \$0 and \$(18) for 2012 and 2011, respectively	-	31
Unrealized gain on available for sale securities		
Unrealized gain on securities, net of tax of \$0 and \$1 for 2012 and 2011, respectively	(4)	(4)
Less: reclassification adjustment for gain on sale of securities included in net income, net of tax of \$8 and \$1 for 2012 and 2011, respectively	(13 )	(2)
Other comprehensive income	(17 )	25
Comprehensive income	\$ 52,971	\$ 49,985

(In thousands)	For the Nine Months Ended September 30,	
	2012	2011
Net income	\$ 159,839	\$ 137,995
Other comprehensive income, net of tax:		
Unrealized loss on derivatives qualifying as hedges		
Unrealized loss on cash flow hedge, net of tax of \$0 and \$6 for 2012 and 2011, respectively	-	(10)
Less: reclassification adjustment for loss on cash flow hedge included in net income, net of tax of \$0 and \$(71) for 2012 and 2011, respectively	-	121
Unrealized gain on available for sale securities		
Unrealized gain on securities, net of tax of \$(8) and \$(1) for 2012 and 2011, respectively	7	3
Less: reclassification adjustment for gain on sale of securities included in net income, net of tax of \$8 and \$1 for 2012 and 2011, respectively	(13 )	(2)
Other comprehensive income	(6 )	112
Comprehensive income	\$ 159,833	\$ 138,107



See accompanying notes to consolidated financial statements.

Table of Contents

CREDIT ACCEPTANCE CORPORATION  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)

(In thousands)	For the Nine Months Ended September 30,	
	2012	2011
Cash Flows From Operating Activities:		
Net income	\$ 159,839	\$ 137,995
Adjustments to reconcile cash provided by operating activities:		
Provision for credit losses	17,716	22,394
Depreciation	3,690	3,076
Amortization	5,126	4,346
Loss on retirement of property and equipment	10	28
Provision for deferred income taxes	11,884	8,763
Stock-based compensation	8,601	1,556
Change in operating assets and liabilities:		
Increase in accounts payable and accrued liabilities	2,273	15,951
Decrease in income taxes receivable	506	11,503
Increase in income taxes payable	8,498	448
Decrease (increase) in other assets	367	(3,703)
Net cash provided by operating activities	218,510	202,357
Cash Flows From Investing Activities:		
Increase in restricted cash and cash equivalents	(63,027)	(24,676)
Purchases of restricted securities available for sale	(100)	(532)
Proceeds from sale of restricted securities available for sale	905	76
Maturities of restricted securities available for sale	–	454
Principal collected on Loans receivable	882,613	748,242
Advances to Dealers	(968,725)	(888,602)
Purchases of Consumer Loans	(85,992)	(94,212)
Accelerated payments of Dealer Holdback	(34,107)	(37,275)
Payments of Dealer Holdback	(89,734)	(58,734)
Net decrease in other loans	84	797
Purchases of property and equipment	(7,091)	(3,569)
Net cash used in investing activities	(365,174)	(358,031)
Cash Flows From Financing Activities:		
Borrowings under revolving secured line of credit	1,969,700	1,757,500
Repayments under revolving secured line of credit	(1,897,800)	(1,794,800)
Proceeds from secured financing	1,426,650	600,000
Repayments of secured financing	(1,234,081)	(385,293)
Principal payments under mortgage note	(184)	(175)
Proceeds from sale of senior notes	–	106,000
Payments of debt issuance costs	(5,973)	(6,849)
Repurchase of common stock	(112,946)	(126,675)
Proceeds from stock options exercised	519	2,781
Tax benefits from stock-based compensation plans	1,847	3,027

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

Net cash provided by financing activities	147,732	155,516
Net increase (decrease) in cash and cash equivalents	1,068	(158)
Cash and cash equivalents, beginning of period	4,657	3,792
Cash and cash equivalents, end of period	\$ 5,725	\$ 3,634
Supplemental Disclosure of Cash Flow Information:		
Cash paid during the period for interest	\$ 49,790	\$ 37,677
Cash paid during the period for income taxes	\$ 68,902	\$ 55,116

See accompanying notes to consolidated financial statements.

Table of Contents

## 1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“generally accepted accounting principles” or “GAAP”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The results of operations for interim periods are not necessarily indicative of actual results achieved for full fiscal years. The consolidated balance sheet as of December 31, 2011 has been derived from the audited financial statements at that date but does not include all the information and footnotes required by GAAP for complete financial statements. For further information, refer to the consolidated financial statements and footnotes thereto included in the Annual Report on Form 10-K for the year ended December 31, 2011 for Credit Acceptance Corporation (the “Company”, “Credit Acceptance”, “we”, “our” or “us”).

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

We have evaluated events and transactions occurring subsequent to the consolidated balance sheet date of September 30, 2012 for items that could potentially be recognized or disclosed in these financial statements. We did not identify any items which would require disclosure in or adjustment to the financial statements, except as disclosed in Note 13 of these consolidated financial statements.

## 2. DESCRIPTION OF BUSINESS

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

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

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

Quarter Ended	Portfolio Program	Purchase Program
March 31, 2011	92.9%	7.1%

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

June 30, 2011	92.1%	7.9%
September 30, 2011	92.3%	7.7%
December 31, 2011	92.6%	7.4%
March 31, 2012	93.3%	6.7%
June 30, 2012	93.6%	6.4%
September 30, 2012	93.8%	6.2%

Table of Contents

2. DESCRIPTION OF BUSINESS – (Continued)

Portfolio Program

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

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

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

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

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

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

Dealers have an opportunity to receive an accelerated Dealer Holdback payment each time 100 Consumer Loans have been assigned to us. The amount paid to the Dealer is calculated using a formula that considers the forecasted collections and the advance balance on the related Consumer Loans.

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

For accounting purposes, the transactions described under the Portfolio Program are not considered to be loans to consumers. Instead, our accounting reflects that of a lender to the Dealer. The classification as a Dealer Loan for accounting purposes is primarily a result of (1) the Dealer’s financial interest in the Consumer Loan and (2) certain elements of our legal relationship with the Dealer.

Purchase Program

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

Table of Contents

## 2. DESCRIPTION OF BUSINESS – (Concluded)

## Program Enrollment

Dealers may enroll in our program by choosing one of our two enrollment options (referred to as “Option A” and “Option B”). In recent years, the terms of Option A have remained consistent while the terms of Option B have varied. The following table summarizes the terms of our enrollment options:

Effective Period	Option A	Option B
Since June 1, 2011	Upfront, one-time fee of \$9,850	Agreement to allow us to retain 50% of their first accelerated Dealer Holdback payment
From September 1, 2009 to May 31, 2011	Upfront, one-time fee of \$9,850	Upfront, one-time fee of \$1,950 and agreement to allow us to retain 50% of their first accelerated Dealer Holdback payment

For Dealers enrolling in our program, access to the Purchase Program is typically only granted after the first accelerated Dealer Holdback payment has been received under the Portfolio Program.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

## Business Segment Information

We currently operate in one reportable segment which represents our core business of offering Dealers financing programs and related products and services that enable them to sell vehicles to consumers, regardless of their credit history. The consolidated financial statements reflect the financial results of our one reportable operating segment.

## Loans Receivable and Allowance for Credit Losses

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



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

Portfolio Segments and Classes. We are considered to be a lender to our Dealers for Consumer Loans assigned under our Portfolio Program and a purchaser of Consumer Loans assigned under our Purchase Program. As a result, our Loan portfolio consists of two portfolio segments: Dealer Loans and Purchased Loans. Each portfolio segment is comprised of one class of Consumer Loan assignments, which is Consumer Loans with deteriorated credit quality that were originated by Dealers to finance consumer purchases of vehicles and related ancillary products.

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

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

Less:

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

Table of Contents

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

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

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

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

- the aggregate amount of all amounts paid during the month of purchase to purchase Consumer Loans from Dealers;
  - finance charges; and
  - recoveries.

Less:

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

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

Future collections on Purchased Loans are forecasted based on the historical performance of Consumer Loans with similar characteristics, adjusted for recent trends in payment patterns. Cash flows from any individual pool of Purchased Loans are often different than estimated cash flows at the time of assignment. If such difference is favorable, the difference is recognized prospectively into income over the remaining life of the pool of Purchased Loans through a yield adjustment. If such difference is unfavorable, a provision for credit losses is recorded immediately as a current period expense and a corresponding allowance for credit losses is established.

Credit Quality. Substantially all of the Consumer Loans assigned to us are made to individuals with impaired or limited credit histories or higher debt-to-income ratios than are permitted by traditional lenders. Consumer Loans made to these individuals generally entail a higher risk of delinquency, default and repossession and higher losses than loans made to consumers with better credit. Since most of our revenue and cash flows are generated from these Consumer Loans, our ability to accurately forecast Consumer Loan performance is critical to our business and financial results. At the time the Consumer Loan is submitted to us for assignment, we forecast future expected cash flows from the Consumer Loan. Based on these forecasts, an advance or one-time purchase payment is made to the related Dealer at a price designed to achieve an acceptable return on capital.

Table of Contents

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

We monitor and evaluate the credit quality of Consumer Loans on a monthly basis by comparing our current forecasted collection rates to our initial expectations. We use a statistical model that considers a number of credit quality indicators to estimate the expected collection rate for each Consumer Loan at the time of assignment. The credit quality indicators considered in our model include attributes contained in the consumer's credit bureau report, data contained in the consumer's credit application, the structure of the proposed transaction, vehicle information and other factors. We continue to evaluate the expected collection rate of each Consumer Loan subsequent to assignment primarily through the monitoring of consumer payment behavior. Our evaluation becomes more accurate as the Consumer Loans age, as we use actual performance data in our forecast. Since all known, significant credit quality indicators have already been factored into our forecasts and pricing, we are not able to use any specific credit quality indicators to predict or explain variances in actual performance from our initial expectations. Any variances in performance from our initial expectations are the result of Consumer Loans performing differently than historical Consumer Loans with similar characteristics. We periodically adjust our statistical pricing model for new trends that we identify through our evaluation of these forecasted collection rate variances.

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

Forecast Methodology Changes and Modifications. For the three and nine months ended September 30, 2012 and 2011, we did not make any methodology changes or significant modifications to our forecasts of future collections on Consumer Loans that had a material impact on our financial results.

## Reinsurance

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

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

(In thousands)	For the Three Months Ended		For the Nine Months Ended	
	September 30,		September 30,	
	2012	2011	2012	2011
Net assumed written premiums	\$ 11,479	\$ 11,293	\$ 39,813	\$ 37,419
Net premiums earned	12,206	10,462	34,987	29,195
Provision for claims	9,122	8,363	26,704	22,733
Amortization of capitalized acquisition costs	342	288	952	747

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

(In thousands)

	Balance Sheet location	As of	
		September 30, 2012	December 31, 2011
Trust assets	Restricted cash and cash equivalents	\$ 48,412	\$ 42,026
Unearned premium	Accounts payable and accrued liabilities	37,161	32,335
Claims reserve (1)	Accounts payable and accrued liabilities	1,515	1,297

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

Table of Contents

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

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

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

## Cash and Cash Equivalents

Cash equivalents consist of readily marketable securities with original maturities at the date of acquisition of three months or less. As of September 30, 2012 and December 31, 2011, we had \$3.5 million and \$4.1 million, respectively, in cash and cash equivalents that were not insured by the Federal Deposit Insurance Corporation ("FDIC").

## Restricted Cash and Cash Equivalents

Restricted cash and cash equivalents increased to \$167.7 million as of September 30, 2012 from \$104.7 million as of December 31, 2011. The following table summarizes restricted cash and cash equivalents:

(In thousands)	As of	
	September 30, 2012	December 31, 2011
Cash related to secured financings	\$119,259	\$62,536
Cash held in trusts for future vehicle service contract claims (1)	48,447	42,143
<b>Total restricted cash and cash equivalents</b>	<b>\$167,706</b>	<b>\$104,679</b>

(1)The unearned premium and claims reserve associated with the trusts are included in accounts payable and accrued liabilities in the consolidated balance sheets. As of September 30, 2012, the outstanding cash balance includes \$48,412 related to VSC Re and \$35 related to a discontinued profit sharing arrangement. As of December 31, 2011, the outstanding cash balance includes \$42,026 related to VSC Re and \$117 related to a discontinued profit sharing arrangement.

As of September 30, 2012 and December 31, 2011, we had \$146.7 million and \$97.5 million, respectively, in restricted cash and cash equivalents that was not insured by the FDIC.



Table of Contents

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

## Restricted Securities Available for Sale

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

Restricted securities available for sale consisted of the following:

(In thousands)	Cost	As of September 30, 2012		Estimated Fair Value
		Gross Unrealized Gains	Gross Unrealized Losses	
Corporate bonds	\$ –	\$ –	\$ –	\$ –

(In thousands)	Cost	As of December 31, 2011		Estimated Fair Value
		Gross Unrealized Gains	Gross Unrealized Losses	
Corporate bonds	\$ 804	\$ 13	\$ (7 )	\$ 810

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

(In thousands)	Cost	As of		Estimated Fair Value
		September 30, 2012 Estimated Fair Value	December 31, 2011 Estimated Fair Value	
Contractual Maturity				
Within one year	\$–	\$–	\$45	\$44
Over one year to five years	–	–	759	766
Total restricted securities available for sale	\$–	\$–	\$804	\$810

## Deferred Debt Issuance Costs

As of September 30, 2012 and December 31, 2011, deferred debt issuance costs were \$18.8 million and \$18.1 million, respectively, and are included in other assets in the consolidated balance sheets. Expenses associated with the issuance of debt instruments are capitalized and amortized as interest expense over the term of the debt instrument using the effective interest method for asset-backed secured financings (“Term ABS”) and 9.125% First Priority Senior Secured Notes due 2017 (“Senior Notes”) and the straight-line method for lines of credit and revolving secured warehouse (“Warehouse”) facilities.





Table of Contents

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Concluded)

Derivative and Hedging Instruments

We rely on various sources of financing, some of which contain floating rates of interest and expose us to risks associated with increases in interest rates. We manage such risk primarily by entering into interest rate cap and interest rate swap agreements (“derivative instruments”).

For derivative instruments that are designated and qualify as hedging instruments, we formally document all relationships between the hedging instruments and hedged items, as well as their risk-management objective and strategy for undertaking various hedge transactions. This process includes linking all derivative instruments that are designated as cash flow hedges to specific assets and liabilities on the balance sheet. We also formally assess (both at the hedge’s inception and on a quarterly basis) whether the derivative instruments that are used in hedging transactions have been highly effective in offsetting changes in the cash flows of hedged items and whether those derivative instruments may be expected to remain highly effective in future periods. The effective portion of changes in the fair value of the derivative instruments is recorded in other comprehensive income, net of income taxes. If it is determined that a derivative instrument is not (or has ceased to be) highly effective as a hedge, we would discontinue hedge accounting prospectively and the ineffective portion of changes in fair value would be recorded in interest expense. For derivative instruments not designated as hedges, changes in the fair value of these agreements increase or decrease interest expense.

We recognize derivative instruments as either other assets or accounts payable and accrued liabilities on our consolidated balance sheets. For additional information regarding our derivative and hedging instruments, see Note 6 to the consolidated financial statements.

New Accounting Updates

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

Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs. In May 2011, the FASB issued ASU No. 2011-04 which amends Topic 820 (Fair Value Measurement). ASU No. 2011-04 is intended to provide a consistent definition of fair value and common requirements for measurement of and disclosure about fair value between U.S. GAAP and IFRS. The amendments in ASU No. 2011-04 include changes regarding how and when the valuation premise of highest and best use applies, the application of premiums and discounts, and new required disclosures. ASU No. 2011-04 is to be applied prospectively upon adoption and is effective for interim and annual periods beginning after December 15, 2011 with early adoption prohibited. The adoption of ASU No. 2011-04 on January 1, 2012 did not have a material impact on our consolidated financial statements, but expanded our disclosures related to fair value measurements.

## 4. LOANS RECEIVABLE

Loans receivable consists of the following:

(In thousands)	As of September 30, 2012		
	Dealer Loans	Purchased Loans	Total
Loans receivable	\$ 1,807,701	\$ 239,780	\$ 2,047,481
Allowance for credit losses	(161,284 )	(9,479 )	(170,763 )
Loans receivable, net	\$ 1,646,417	\$ 230,301	\$ 1,876,718

(In thousands)	As of December 31, 2011		
	Dealer Loans	Purchased Loans	Total
Loans receivable	\$ 1,506,539	\$ 246,352	\$ 1,752,891
Allowance for credit losses	(141,712 )	(12,606 )	(154,318 )
Loans receivable, net	\$ 1,364,827	\$ 233,746	\$ 1,598,573

Table of Contents

## 4. LOANS RECEIVABLE – (Continued)

A summary of changes in Loans receivable is as follows:

	For the Three Months Ended September 30, 2012		
	Purchased		Total
	Dealer Loans	Loans	
Balance, beginning of period	\$ 1,736,578	\$ 241,216	\$ 1,977,794
New Consumer Loan assignments (1)	293,379	25,238	318,617
Principal collected on Loans receivable	(252,398)	(32,617)	(285,015)
Accelerated Dealer Holdback payments	9,884	–	9,884
Dealer Holdback payments	27,118	–	27,118
Transfers (2)	(5,946)	5,946	–
Write-offs	(1,480)	(26)	(1,506)
Recoveries (3)	582	23	605
Net change in other loans	(16)	–	(16)
Balance, end of period	\$ 1,807,701	\$ 239,780	\$ 2,047,481

	For the Three Months Ended September 30, 2011		
	Purchased		Total
	Dealer Loans	Loans	
Balance, beginning of period	\$ 1,331,973	\$ 250,932	\$ 1,582,905
New Consumer Loan assignments (1)	278,395	30,717	309,112
Principal collected on Loans receivable	(216,860)	(36,970)	(253,830)
Accelerated Dealer Holdback payments	12,859	–	12,859
Dealer Holdback payments	23,985	–	23,985
Transfers (2)	(2,933)	2,933	–
Write-offs	(736)	(68)	(804)
Recoveries (3)	442	21	463
Net change in other loans	(259)	–	(259)
Balance, end of period	\$ 1,426,866	\$ 247,565	\$ 1,674,431

	For the Nine Months Ended September 30, 2012		
	Dealer	Purchased	Total
	Loans	Loans	
Balance, beginning of period	\$ 1,506,539	\$ 246,352	\$ 1,752,891
New Consumer Loan assignments (1)	968,725	85,992	1,054,717
Principal collected on Loans receivable	(774,361)	(108,252)	(882,613)
Accelerated Dealer Holdback payments	34,107	–	34,107
Dealer Holdback payments	89,734	–	89,734
Transfers (2)	(16,150)	16,150	–
Write-offs	(2,483)	(532)	(3,015)
Recoveries (3)	1,674	70	1,744
Net change in other loans	(84)	–	(84)
Balance, end of period	\$ 1,807,701	\$ 239,780	\$ 2,047,481

(In thousands)

	For the Nine Months Ended September 30, 2011		
	Dealer Loans	Purchased Loans	Total
Balance, beginning of period	\$ 1,082,039	\$ 262,842	\$ 1,344,881
New Consumer Loan assignments (1)	888,602	94,212	982,814
Principal collected on Loans receivable	(628,406)	(119,836)	(748,242)
Accelerated Dealer Holdback payments	37,275	–	37,275
Dealer Holdback payments	58,734	–	58,734
Transfers (2)	(10,490)	10,490	–
Write-offs	(1,563)	(207)	(1,770)
Recoveries (3)	1,472	64	1,536
Net change in other loans	(797)	–	(797)
Balance, end of period	\$ 1,426,866	\$ 247,565	\$ 1,674,431

- (1) The Dealer Loans amount represents advances paid to Dealers on Consumer Loans assigned under our Portfolio Program. The Purchased Loans amount represents one-time payments made to Dealers to purchase Consumer Loans assigned under our Purchase Program.
- (2) Under our Portfolio Program, certain events may result in Dealers forfeiting their rights to Dealer Holdback. We transfer the Dealer's outstanding Dealer Loan balance to Purchased Loans in the period this forfeiture occurs.
- (3) Represents collections received on previously written off Loans.

Table of Contents

## 4. LOANS RECEIVABLE – (Continued)

Contractual net cash flows are comprised of the contractual repayments of the underlying Consumer Loans for Dealer and Purchased Loans, less the related Dealer Holdback payments for Dealer Loans. The difference between the contractual net cash flows and the expected net cash flows is referred to as the nonaccretable difference. This difference is neither accreted into income nor recorded in our balance sheets. We do not believe that the contractual net cash flows of our Loan portfolio are relevant in assessing our financial position. We are contractually owed repayments on many Consumer Loans, primarily those older than 120 months, where we are not forecasting any future net cash flows.

The excess of expected net cash flows over the carrying value of the Loans is referred to as the accretable yield and is recognized on a level-yield basis as finance charge income over the remaining lives of the Loans. A summary of changes in the accretable yield is as follows:

(In thousands)	For the Three Months Ended September 30, 2012		
	Dealer Loans	Purchased Loans	Total
Balance, beginning of period	\$ 581,693	\$ 119,493	\$ 701,186
New Consumer Loan assignments (1)	127,728	10,790	138,518
Finance charge income	(117,780)	(19,715)	(137,495)
Forecast changes	6,880	1,265	8,145
Transfers (2)	(2,580)	4,240	1,660
Balance, end of period	\$ 595,941	\$ 116,073	\$ 712,014

(In thousands)	For the Three Months Ended September 30, 2011		
	Dealer Loans	Purchased Loans	Total
Balance, beginning of period	\$ 462,478	\$ 123,561	\$ 586,039
New Consumer Loan assignments (1)	122,010	14,125	136,135
Finance charge income	(96,577)	(21,328)	(117,905)
Forecast changes	5,211	2,791	8,002
Transfers (2)	(1,349)	2,182	833
Balance, end of period	\$ 491,773	\$ 121,331	\$ 613,104

(In thousands)	For the Nine Months Ended September 30, 2012		
	Dealer Loans	Purchased Loans	Total
Balance, beginning of period	\$ 508,046	\$ 120,082	\$ 628,128
New Consumer Loan assignments (1)	416,159	38,227	454,386
Finance charge income	(337,231)	(60,332)	(397,563)
Forecast changes	16,322	6,406	22,728
Transfers (2)	(7,355)	11,690	4,335
Balance, end of period	\$ 595,941	\$ 116,073	\$ 712,014

(In thousands)	For the Nine Months Ended September 30, 2011		
	Dealer Loans	Purchased Loans	Total
Balance, beginning of period	\$ 351,569	\$ 124,520	\$ 476,089

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

New Consumer Loan assignments (1)	395,111	46,627	441,738
Finance charge income	(273,300)	(64,938)	(338,238)
Forecast changes	23,440	6,659	30,099
Transfers (2)	(5,047)	8,463	3,416
Balance, end of period	\$ 491,773	\$ 121,331	\$ 613,104

- (1) The Dealer Loans amount represents the net cash flows expected at the time of assignment on Consumer Loans assigned under our Portfolio Program, less the related advances paid to Dealers. The Purchased Loans amount represents the net cash flows expected at the time of assignment on Consumer Loans assigned under our Purchase Program, less the related one-time payments made to Dealers.
- (2) Under our Portfolio Program, certain events may result in Dealers forfeiting their rights to Dealer Holdback. We transfer the Dealer's outstanding Dealer Loan balance and related expected future net cash flows to Purchased Loans in the period this forfeiture occurs.

Table of Contents

## 4. LOANS RECEIVABLE – (Continued)

Additional information related to new Consumer Loan assignments is as follows:

(In thousands)	For the Three Months Ended September 30, 2012		
	Dealer	Purchased	Total
	Loans	Loans	
Contractual net cash flows at the time of assignment (1)	\$ 454,859	\$ 50,278	\$ 505,137
Expected net cash flows at the time of assignment (2)	421,107	36,028	457,135
Fair value at the time of assignment (3)	293,379	25,238	318,617

(In thousands)	For the Three Months Ended September 30, 2011		
	Dealer	Purchased	Total
	Loans	Loans	
Contractual net cash flows at the time of assignment (1)	\$ 431,399	\$ 61,382	\$ 492,781
Expected net cash flows at the time of assignment (2)	400,405	44,842	445,247
Fair value at the time of assignment (3)	278,395	30,717	309,112

(In thousands)	For the Nine Months Ended September 30, 2012		
	Dealer Loans	Purchased	Total
		Loans	
Contractual net cash flows at the time of assignment (1)	\$ 1,495,980	\$ 173,176	\$ 1,669,156
Expected net cash flows at the time of assignment (2)	1,384,884	124,219	1,509,103
Fair value at the time of assignment (3)	968,725	85,992	1,054,717

(In thousands)	For the Nine Months Ended September 30, 2011		
	Dealer Loans	Purchased	Total
		Loans	
Contractual net cash flows at the time of assignment (1)	\$ 1,378,850	\$ 191,814	\$ 1,570,664
Expected net cash flows at the time of assignment (2)	1,283,713	140,839	1,424,552
Fair value at the time of assignment (3)	888,602	94,212	982,814

(1) The Dealer Loans amount represents the repayments that we were contractually owed at the time of assignment on Consumer Loans assigned under our Portfolio Program, less the related Dealer Holdback payments that we would be required to make if we collected all of the contractual repayments. The Purchased Loans amount represents the repayments that we were contractually owed at the time of assignment on Consumer Loans assigned under our Purchase Program.

(2) The Dealer Loans amount represents the repayments that we expected to collect at the time of assignment on Consumer Loans assigned under our Portfolio Program, less the related Dealer Holdback payments that we expected to make. The Purchased Loans amount represents the repayments that we expected to collect at the time of assignment on Consumer Loans assigned under our Purchase Program.

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





Table of Contents

## 4. LOANS RECEIVABLE – (Continued)

## Credit Quality

We monitor and evaluate the credit quality of Consumer Loans assigned under our Portfolio and Purchase Programs on a monthly basis by comparing our current forecasted collection rates to our initial expectations. For additional information regarding credit quality, see Note 3 to the consolidated financial statements. The following table compares our forecast of Consumer Loan collection rates as of September 30, 2012, with the forecasts as of June 30, 2012, as of December 31, 2011, and at the time of assignment, segmented by year of assignment:

Consumer Loan Assignment Year	Forecasted Collection Percentage as of (1)				Variance in Forecasted Collection Percentage from		
	September 30, 2012	June 30, 2012	December 31, 2011	Initial Forecast	June 30, 2012	December 31, 2011	Initial Forecast
2003	73.8%	73.8%	73.7%	72.0%	0.0%	0.1%	1.8%
2004	73.0%	73.0%	73.0%	73.0%	0.0%	0.0%	0.0%
2005	73.5%	73.6%	73.6%	74.0%	-0.1%	-0.1%	-0.5%
2006	70.0%	70.0%	70.0%	71.4%	0.0%	0.0%	-1.4%
2007	68.1%	68.1%	68.1%	70.7%	0.0%	0.0%	-2.6%
2008	70.3%	70.3%	70.0%	69.7%	0.0%	0.3%	0.6%
2009	79.5%	79.6%	79.4%	71.9%	-0.1%	0.1%	7.6%
2010	77.2%	77.1%	76.8%	73.6%	0.1%	0.4%	3.6%
2011	73.7%	73.6%	73.2%	72.5%	0.1%	0.5%	1.2%
2012 (2)	71.6%	71.9%	–	71.1%	-0.3%	–	0.5%

- (1) Represents the total forecasted collections we expect to collect on the Consumer Loans as a percentage of the repayments that we were contractually owed on the Consumer Loans at the time of assignment. Contractual repayments include both principal and interest.
- (2) The forecasted collection rate for 2012 Consumer Loans as of September 30, 2012 includes both Consumer Loans that were in our portfolio as of June 30, 2012 and Consumer Loans assigned during the most recent quarter. The following table provides forecasted collection rates for each of these segments:

2012 Consumer Loan Assignment Period	Forecasted Collection Percentage as of		Variance
	September 30, 2012	June 30, 2012	
January 1, 2012 through June 30, 2012	72.0	% 71.9	% 0.1
July 1, 2012 through September 30, 2012	70.6	% –	–

Advances paid to Dealers on Consumer Loans assigned under our Portfolio Program and one-time payments made to Dealers to purchase Consumer Loans assigned under our Purchase Program are aggregated into pools for purposes of recognizing revenue and evaluating impairment. As a result of this aggregation, we are not able to segment the carrying value of the majority of our Loan portfolio by year of assignment. The following table summarizes Loan pools based on the performance of the underlying pool of Consumer Loans:

(In thousands)	As of September 30, 2012	
	Loan Pool Performance Meets or Exceeds Initial Estimates	Loan Pool Performance Less than Initial Estimates

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

	Dealer Loans	Purchased Loans	Total	Dealer Loans	Purchased Loans	Total
Loans receivable	\$ 572,223	\$ 196,367	\$ 768,590	\$ 1,235,479	\$ 43,413	\$ 1,278,892
Allowance for credit losses	–	–	–	(161,284 )	(9,479 )	(170,763 )
Loans receivable, net	\$ 572,223	\$ 196,367	\$ 768,590	\$ 1,074,195	\$ 33,934	\$ 1,108,129

(In thousands)

As of December 31, 2011

	Loan Pool Performance Meets or Exceeds Initial Estimates			Loan Pool Performance Less than Initial Estimates		
	Dealer Loans	Purchased Loans	Total	Dealer Loans	Purchased Loans	Total
	Loans receivable	\$ 511,926	\$ 192,502	\$ 704,428	\$ 994,613	\$ 53,850
Allowance for credit losses	–	–	–	(141,712 )	(12,606 )	(154,318 )
Loans receivable, net	\$ 511,926	\$ 192,502	\$ 704,428	\$ 852,901	\$ 41,244	\$ 894,145

Table of Contents

## 4. LOANS RECEIVABLE – (Concluded)

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

(In thousands)	For the Three Months Ended September 30, 2012		
	Purchased		Total
	Dealer Loans	Loans	
Balance, beginning of period	\$ 152,031	\$ 9,874	\$ 161,905
Provision for credit losses	10,151	(392)	9,759
Write-offs	(1,480)	(26)	(1,506)
Recoveries (1)	582	23	605
Balance, end of period	\$ 161,284	\$ 9,479	\$ 170,763

(In thousands)	For the Three Months Ended September 30, 2011		
	Purchased		Total
	Dealer Loans	Loans	
Balance, beginning of period	\$ 131,728	\$ 13,091	\$ 144,819
Provision for credit losses	4,723	(173)	4,550
Write-offs	(736)	(68)	(804)
Recoveries (1)	442	21	463
Balance, end of period	\$ 136,157	\$ 12,871	\$ 149,028

(In thousands)	For the Nine Months Ended September 30, 2012		
	Dealer	Purchased	Total
	Loans	Loans	
Balance, beginning of period	\$ 141,712	\$ 12,606	\$ 154,318
Provision for credit losses	20,381	(2,665)	17,716
Write-offs	(2,483)	(532)	(3,015)
Recoveries (1)	1,674	70	1,744
Balance, end of period	\$ 161,284	\$ 9,479	\$ 170,763

(In thousands)	For the Nine Months Ended September 30, 2011		
	Dealer	Purchased	Total
	Loans	Loans	
Balance, beginning of period	\$ 113,227	\$ 13,641	\$ 126,868
Provision for credit losses	23,021	(627)	22,394
Write-offs	(1,563)	(207)	(1,770)
Recoveries (1)	1,472	64	1,536
Balance, end of period	\$ 136,157	\$ 12,871	\$ 149,028

(1) Represents collections received on previously written off Loans.



Table of Contents

## 5. DEBT

We currently utilize the following primary forms of debt financing: (1) a revolving secured line of credit; (2) Warehouse facilities; (3) Term ABS financings and (4) Senior Notes. General information for each of our financing transactions in place as of September 30, 2012 is as follows:

(Dollars in thousands)

Financings	Wholly-owned Subsidiary	Close Date	Maturity Date	Financing Amount	Interest Rate as of September 30, 2012
Revolving Secured Line of Credit	n/a	06/15/2012	06/22/2015	\$ 235,000	At our option, either LIBOR plus 187.5 basis points or the prime rate plus 87.5 basis points
Warehouse Facility II (1)	CAC Warehouse Funding Corp. II	06/17/2011	06/17/2014 (2)	\$ 325,000	Commercial paper rate plus 275 basis points or LIBOR plus 375 basis points (3) (4)
Warehouse Facility III (1)	CAC Warehouse Funding III, LLC	06/29/2012	09/10/2015 (5)	\$ 75,000	LIBOR plus 160 basis points (4)
Warehouse Facility IV (1)	CAC Warehouse Funding LLC IV	08/19/2011	02/19/2014 (2)	\$ 75,000	LIBOR plus 275 basis points (4)
Term ABS 2010-1 (1)	Credit Acceptance Funding LLC 2010-1	11/04/2010	10/15/2012 (2)	\$ 100,500	Fixed rate
Term ABS 2011-1 (1)	Credit Acceptance Funding LLC 2011-1	10/06/2011	09/16/2013 (2)	\$ 200,500	Fixed rate
Term ABS 2012-1 (1)	Credit Acceptance Funding LLC 2012-1	03/29/2012	03/17/2014 (2)	\$ 201,250	Fixed rate
Term ABS 2012-2 (1)	Credit Acceptance Funding LLC 2012-2	09/20/2012	09/15/2014 (2)	\$ 252,000	Fixed rate
Senior Notes	n/a	(6)	02/01/2017	\$ 350,000	Fixed rate

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

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

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

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

(5)

Represents the revolving maturity date. The outstanding balance will amortize after the revolving maturity date and any amounts remaining on September 10, 2017 will be due.

(6) The close dates associated with the issuance of \$250.0 million and \$100.0 million of the Senior Notes were on February 1, 2010 and March 3, 2011, respectively.

Table of Contents

## 5. DEBT – (Continued)

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

(In thousands)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2012	2011	2012	2011
<b>Revolving Secured Line of Credit</b>				
Maximum outstanding balance	\$ 139,000	\$ 165,400	\$ 187,300	\$ 165,400
Average outstanding balance	100,133	113,098	98,876	108,262
<b>Warehouse Facility II</b>				
Maximum outstanding balance	\$ 173,800	\$ 264,000	\$ 177,200	\$ 264,000
Average outstanding balance	143,733	215,522	128,606	184,224
<b>Warehouse Facility III</b>				
Maximum outstanding balance	\$ 62,000	\$ 75,000	\$ 73,000	\$ 75,000
Average outstanding balance	51,423	73,587	60,760	47,436
<b>Warehouse Facility IV</b>				
Maximum outstanding balance	\$ 39,200	\$ 43,500	\$ 39,600	\$ 43,500
Average outstanding balance	37,809	41,895	37,847	41,895



Table of Contents

## 5. DEBT – (Continued)

(Dollars in thousands)

	As of	
	September 30, 2012	December 31, 2011
<b>Revolving Secured Line of Credit</b>		
Balance outstanding	\$ 115,800	\$ 43,900
Amount available for borrowing (1)	119,200	161,100
Interest rate	2.09%	2.55%
<b>Warehouse Facility II</b>		
Balance outstanding	\$ –	\$ 163,200
Amount available for borrowing (1)	325,000	161,800
Loans pledged as collateral	–	242,119
Restricted cash and cash equivalents pledged as collateral	1,626	6,117
Interest rate	2.96%	2.99%
<b>Warehouse Facility III</b>		
Balance outstanding	\$ –	\$ 70,000
Amount available for borrowing (1)	75,000	5,000
Loans pledged as collateral	–	91,601
Restricted cash and cash equivalents pledged as collateral	538	3,321
Interest rate	1.82%	1.89%
<b>Warehouse Facility IV</b>		
Balance outstanding	\$ 37,600	\$ 37,500
Amount available for borrowing (1)	37,400	37,500
Loans pledged as collateral	49,003	62,260
Restricted cash and cash equivalents pledged as collateral	2,843	2,188
Interest rate	2.97%	3.05%
<b>Term ABS 2009-1</b>		
Balance outstanding	\$ –	\$ 27,581
Loans pledged as collateral	–	105,209
Restricted cash and cash equivalents pledged as collateral	–	13,526
Interest rate	–	5.68%
<b>Term ABS 2010-1</b>		
Balance outstanding	\$ 100,500	\$ 100,500
Loans pledged as collateral	123,609	125,541
Restricted cash and cash equivalents pledged as collateral	14,288	14,116
Interest rate	2.36%	2.36%
<b>Term ABS 2011-1</b>		
Balance outstanding	\$ 200,500	\$ 200,500
Loans pledged as collateral	244,531	248,167
Restricted cash and cash equivalents pledged as collateral	25,300	23,268
Interest rate	2.90%	2.90%

## Term ABS 2012-1

Balance outstanding	\$ 201,250	\$	–
Loans pledged as collateral	246,756		–
Restricted cash and cash equivalents pledged as collateral	23,561		–
Interest rate	2.38%		–

## Term ABS 2012-2

Balance outstanding	\$ 252,000	\$	–
Loans pledged as collateral	312,152		–
Restricted cash and cash equivalents pledged as collateral	51,103		–
Interest rate	1.63%		–

## Senior Notes

Balance outstanding (2)	\$ 350,307	\$	350,378
Interest rate	9.13%		9.13%

(1) Availability may be limited by the amount of assets pledged as collateral.

(2) As of September 30, 2012 and December 31, 2011, the outstanding balance presented for the Senior Notes includes a net unamortized debt premium of \$0.3 million and \$0.4 million, respectively.

Table of Contents

5. DEBT – (Continued)

Revolving Secured Line of Credit Facility

We have a \$235.0 million revolving secured line of credit facility with a commercial bank syndicate.

During the second quarter of 2012, we extended the maturity of our revolving secured line of credit facility from June 22, 2014 to June 22, 2015. Additionally, the amount of the facility was increased from \$205.0 million to \$235.0 million. The interest rate on borrowings under the facility was decreased from the prime rate plus 1.25% or the LIBOR rate plus 2.25%, at our option, to the prime rate plus 0.875% or the LIBOR rate plus 1.875%, at our option.

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

Warehouse Facilities

We have three Warehouse facilities with total borrowing capacity of \$475.0 million. Each of the facilities are with different institutional investors, and the facility limit is \$325.0 million for Warehouse Facility II and \$75.0 million for both Warehouse Facility III and IV.

During the second quarter of 2012, we extended the date on which Warehouse III will cease to revolve from September 10, 2013 to September 10, 2015. The maturity of the facility was also extended from September 10, 2014 to September 10, 2017. There were no other material changes to the terms of the facility.

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

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

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

Term ABS Financings

In 2009, 2010, 2011 and 2012, five of our wholly-owned subsidiaries (the “Funding LLCs”), completed secured financing transactions with qualified institutional investors. In connection with these transactions, we contributed Loans on an arms-length basis to each Funding LLC for cash and the sole membership interest in that Funding LLC. In turn, each Funding LLC contributed the Loans to a respective trust that issued notes to qualified institutional investors. The Term ABS 2009-1 ceased to revolve on May 15, 2011 and was paid in full during the first quarter of 2012. The Term ABS 2010-1, 2011-1, 2012-1 and 2012-2 transactions each consist of three classes of notes. The Class A and Class B Notes for each Term ABS financing bear interest. The Class C Notes for each Term ABS financing do not bear interest and have been retained by us.

Table of Contents

## 5. DEBT – (Continued)

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

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

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

(Dollars in thousands)

Term ABS Financings	Close Date	Net Book Value of Loans Contributed at Closing	Revolving Period
Term ABS 2010-1	November 4, 2010	\$ 126,751	24 months (Through October 15, 2012)
Term ABS 2011-1	October 6, 2011	\$ 250,827	24 months (Through September 16, 2013)
Term ABS 2012-1	March 29, 2012	\$ 251,681	24 months (Through March 17, 2014)
Term ABS 2012-2	September 20, 2012	\$ 315,120	24 months (Through September 15, 2014)

## Senior Notes

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

The Senior Notes mature on February 1, 2017 and bear interest at a rate of 9.125% per annum, computed on the basis of a 360-day year comprised of twelve 30-day months and payable semi-annually on February 1 and August 1 of each year. The Senior Notes issued on March 3, 2011 were issued at a price of 106.0% of their aggregate principal amount, resulting in gross proceeds of \$106.0 million, and a yield to maturity of 7.83% per annum. The Senior Notes issued

on February 1, 2010 were issued at a price of 97.495% of their aggregate principal amount, resulting in gross proceeds of \$243.7 million, and a yield to maturity of 9.625% per annum. The premium with respect to the Senior Notes issued on March 3, 2011 and the discount with respect to the Senior Notes issued on February 1, 2010 are being amortized over the life of the Senior Notes using the effective interest method.

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

Table of Contents

## 5. DEBT – (Concluded)

## Debt Covenants

As of September 30, 2012, we were in compliance with all our debt covenants relating to the revolving secured line of credit facility, including those that require the maintenance of certain financial ratios and other financial conditions. These covenants require a minimum ratio of our earnings before interest, taxes and non-cash expenses to fixed charges. These covenants also limit the maximum ratio of our funded debt to tangible net worth. Additionally, we must maintain consolidated net income of not less than \$1 for the two most recently ended fiscal quarters. Some of these debt covenants may indirectly limit the repurchase of common stock or payment of dividends on common stock.

Our Warehouse facilities and Term ABS financings also contain covenants that measure the performance of the contributed assets. As of September 30, 2012, we were in compliance with all such covenants. As of the end of the quarter, we were also in compliance with our covenants under the Indenture. The Indenture includes covenants that limit the maximum ratio of our funded debt to tangible net worth and also require a minimum collateral coverage ratio.

## 6. DERIVATIVE AND HEDGING INSTRUMENTS

Interest Rate Caps. We utilize interest rate cap agreements to manage the interest rate risk on our Warehouse facilities. The following tables provide the terms of our interest rate cap agreements that were in effect as of September 30, 2012 and December 31, 2011:

## As of September 30, 2012

Facility (in millions)	Facility Name	Purpose	Start	End	Notional (in millions)	Cap Interest Rate (1)
\$ 325.0	Warehouse Facility II	Cap Floating Rate	07/2011	06/2013	\$ 325.0	6.75%
75.0	Warehouse Facility III	Cap Floating Rate	09/2010	09/2013	37.5	6.75%
75.0	Warehouse Facility III	Cap Floating Rate	06/2012	07/2015	18.8 (2)	5.00%
75.0	Warehouse Facility IV	Cap Floating Rate	08/2011	03/2014	75.0	5.50%

## As of December 31, 2011

Facility (in millions)	Facility Name	Purpose	Start	End	Notional (in millions)	Cap Interest Rate (1)
\$ 325.0	Warehouse Facility II	Cap Floating Rate	09/2010	06/2013	\$ 325.0	6.75%
75.0	Warehouse Facility III	Cap Floating Rate	09/2010	09/2013	37.5	6.75%
75.0	Warehouse Facility IV	Cap Floating Rate	08/2011	03/2014	75.0	5.50%

(1) Rate excludes the spread over the LIBOR rate or the commercial paper rate, as applicable.

- (2) The notional amount increases to \$56.3 million in September 2013 when the original Warehouse Facility III interest rate cap for \$37.5 million ends.

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

Information related to the fair values of derivative instruments in our consolidated balance sheets as of September 30, 2012 and December 31, 2011 is as follows:

(In thousands)	Balance Sheet location	Fair Value as of	
		September 30, 2012	December 31, 2011
Derivatives not designated as hedging instruments			
Asset Derivatives			
Interest rate caps	Other assets	\$ 18	\$ 16



Table of Contents

## 6. DERIVATIVE AND HEDGING INSTRUMENTS – (Concluded)

Information related to the effect of derivative instruments designated as hedging instruments in our consolidated financial statements for the three and nine months ended September 30, 2012 and 2011 is as follows:

(In thousands)

Derivatives in Cash Flow Hedging Relationships	(Loss) / Gain Recognized in OCI on Derivative (Effective Portion) For the Three Months Ended September 30,		Location	(Loss) / Gain Reclassified from Accumulated OCI into Income (Effective Portion) For the Three Months Ended September 30,		
	2012	2011		2012	2011	
Interest rate swap	\$	–	\$	–	\$	(49)

(In thousands)

Derivatives in Cash Flow Hedging Relationships	(Loss) / Gain Recognized in OCI on Derivative (Effective Portion) For the Nine Months Ended September 30,		Location	(Loss) / Gain Reclassified from Accumulated OCI into Income (Effective Portion) For the Nine Months Ended September 30,		
	2012	2011		2012	2011	
Interest rate swap	\$	–	\$	(16)	\$	(192)

Information related to the effect of derivative instruments not designated as hedging instruments on our consolidated statements of income for the three and nine months ended September 30, 2012 and 2011 is as follows:

(In thousands)

Derivatives Not Designated as Hedging Instruments	Location	Amount of (Loss) / Gain Recognized in Income on Derivatives For the Three Months Ended September 30,		Amount of (Loss) / Gain Recognized in Income on Derivatives For the Nine Months Ended September 30,			
		2012	2011	2012	2011		
Interest rate caps	Interest expense	\$	(7)	\$	(66)	\$	(202)

## 7. FAIR VALUE OF FINANCIAL INSTRUMENTS

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

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

**Restricted Securities Available for Sale.** Restricted securities consist of amounts held in trusts by TPAs to pay claims on vehicle service contracts. Securities for which we do not have the intent or ability to hold to maturity are classified

as available for sale and stated at fair value. The fair value of restricted securities are based on quoted market values.

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

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

Liabilities. The fair value of our Senior Notes is determined using quoted market prices in an active market. The fair value of our Term ABS financings is also determined using quoted market prices, however, these instruments trade in a market with much lower trading volume. For our Revolving Secured Line of Credit, our Warehouse Facilities and our mortgage note, the fair values are calculated using the estimated value of each debt instrument based on current rates for debt with similar risk profiles and maturities.

Table of Contents

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

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

(In thousands)

	As of September 30, 2012		As of December 31, 2011	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
<b>Assets</b>				
Cash and cash equivalents	\$ 5,725	\$ 5,725	\$ 4,657	\$ 4,657
Restricted cash and cash equivalents	167,706	167,706	104,679	104,679
Restricted securities available for sale	–	–	810	810
Net investment in Loans receivable	1,876,718	1,895,056	1,598,573	1,615,009
Derivative instruments	18	18	16	16
<b>Liabilities</b>				
Revolving secured line of credit	\$ 115,800	\$ 115,800	\$ 43,900	\$ 43,900
Secured financing	791,850	801,226	599,281	598,622
Mortgage note	4,104	4,104	4,288	4,288
Senior notes	350,307	385,875	350,378	365,500

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

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

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

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

Table of Contents

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

The following table provides the level of measurement used to determine the fair value for each of our financial instruments on a recurring basis, as of September 30, 2012 and December 31, 2011:

(In thousands)

	As of September 30, 2012			Total Fair Value
	Level 1	Level 2	Level 3	
<b>Assets</b>				
Cash and cash equivalents	\$5,725	\$–	\$–	\$5,725
Restricted cash and cash equivalents	167,706	–	–	167,706
Restricted securities available for sale	–	–	–	–
Net investment in Loans receivable	–	–	1,895,056	1,895,056
Derivative instruments	–	18	–	18
<b>Liabilities</b>				
Revolving secured line of credit	\$–	\$115,800	\$–	\$115,800
Secured financing	–	801,226	–	801,226
Mortgage note	–	4,104	–	4,104
Senior notes	385,875	–	–	385,875

(In thousands)

	As of December 31, 2011			Total Fair Value
	Level 1	Level 2	Level 3	
<b>Assets</b>				
Cash and cash equivalents	\$4,657	\$–	\$–	\$4,657
Restricted cash and cash equivalents	104,679	–	–	104,679
Restricted securities available for sale	810	–	–	810
Net investment in Loans receivable	–	–	1,615,009	1,615,009
Derivative instruments	–	16	–	16
<b>Liabilities</b>				
Revolving secured line of credit	\$–	\$43,900	\$–	\$43,900
Secured financing	–	598,622	–	598,622
Mortgage note	–	4,288	–	4,288
Senior notes	365,500	–	–	365,500

Table of Contents

## 8. RELATED PARTY TRANSACTIONS

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

Affiliated Dealer Loan balances were \$5.6 million and \$4.9 million as of September 30, 2012 and December 31, 2011, respectively. As of September 30, 2012 and December 31, 2011, affiliated Dealer Loan balances were 0.3% of total consolidated Dealer Loan balances. A summary of related party Loan activity is as follows:

(In thousands)	For the Three Months Ended September 30,			
	2012		2011	
	Affiliated Dealer activity	% of consolidated	Affiliated Dealer activity	% of consolidated
Dealer Loan revenue	\$ 284	0.2 %	\$ 349	0.4 %
New Consumer Loan assignments (1)	928	0.3 %	128	0.0 %
Accelerated Dealer Holdback payments	79	0.8 %	–	0.0 %
Dealer Holdback payments	692	2.6 %	652	2.7 %

(In thousands)	For the Nine Months Ended September 30,			
	2012		2011	
	Affiliated Dealer activity	% of consolidated	Affiliated Dealer activity	% of consolidated
Dealer Loan revenue	\$ 849	0.2 %	\$ 1,330	0.5 %
New Consumer Loan assignments (1)	2,662	0.3 %	788	0.1 %
Accelerated Dealer Holdback payments	149	0.4 %	24	0.1 %
Dealer Holdback payments	2,643	2.9 %	1,757	3.0 %

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

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

## 9. INCOME TAXES

A reconciliation of the U.S. federal statutory rate to our effective tax rate is as follows:

	For the Three Months Ended September 30,	For the Nine Months Ended September 30,

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

	2012	2011	2012	2011
U.S. federal statutory rate	35.0%	35.0%	35.0%	35.0%
State income taxes	1.7%	1.5%	1.6%	1.9%
Changes in reserve for uncertain tax positions as a result of settlements and lapsed statutes and related interest	-0.4%	-0.2%	-0.4%	-0.6%
Other	0.5%	0.2%	0.3%	0.0%
Effective tax rate	36.8%	36.5%	36.5%	36.3%

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

Table of Contents

## 10. NET INCOME PER SHARE

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

(In thousands)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2012	2011	2012	2011
Weighted average shares outstanding:				
Common shares	24,337	25,605	25,074	25,991
Vested restricted stock units	571	428	555	406
Basic number of weighted average shares outstanding	24,908	26,033	25,629	26,397
Dilutive effect of stock options	46	70	50	116
Dilutive effect of restricted stock and restricted stock units	8	33	27	60
Dilutive number of weighted average shares outstanding	24,962	26,136	25,706	26,573

For the three and nine months ended September 30, 2012 and 2011, there were no stock options, restricted stock or restricted stock units that would have been anti-dilutive.

## 11. STOCK REPURCHASES

On August 5, 1999, our board of directors approved a stock repurchase program which authorizes us to repurchase common shares in the open market or in privately negotiated transactions at price levels we deem attractive. On March 26, 2012, the board of directors authorized the repurchase of up to one million shares of our common stock in addition to the board's prior authorizations. As of September 30, 2012, we had authorization to repurchase 976,129 shares of our common stock.

During the first two quarters of 2012, we repurchased 285,402 shares of our common stock in the open market at a cost of \$27.0 million.

During the second quarter of 2012, we commenced a tender offer to repurchase 1.0 million shares of our common stock at a price of \$84.45 per share. Upon expiration of the tender offer during the second quarter of 2012, we repurchased 1.0 million common shares at a cost of \$84.5 million. The settlement during the third quarter of 2012 was financed by borrowing under our revolving secured line of credit facility.

During the first quarter of 2011, we commenced a tender offer to repurchase 1.9 million shares of our common stock at a price of \$65.625 per share. Upon expiration of the tender offer during the first quarter of 2011, we repurchased 1.9 million common shares at a cost of \$125.0 million. We financed the repurchase of our common stock in the tender offer using the proceeds from the issuance of \$100.0 million of Senior Notes and by borrowing under our revolving secured line of credit facility.

## 12. STOCK-BASED COMPENSATION PLANS

On March 26, 2012, our board of directors approved an amendment to our Amended and Restated Incentive Compensation Plan (the "Incentive Plan") increasing the number of shares authorized for issuance by 500,000 shares, to 2 million shares. Pursuant to the Incentive Plan, we can grant restricted stock, restricted stock units, stock options,

and performance awards to team members, officers, directors, and contractors at any time prior to March 26, 2022. The shares available for future grants under the Incentive Plan totaled 342,300 as of September 30, 2012.

On March 26, 2012, the compensation committee of our board of directors approved an award of 310,000 restricted stock units and 190,000 shares of restricted stock to our Chief Executive Officer. The 310,000 restricted stock units and 90,000 shares of restricted stock are eligible to vest over a ten year period beginning in 2012 based on the cumulative improvement in our annual adjusted economic profit, a non-GAAP financial measure. The remaining 100,000 shares of restricted stock are eligible to vest in equal annual installments over a five year period beginning in 2022 based on the attainment of annual adjusted economic profit targets.



Table of Contents

## 12. STOCK-BASED COMPENSATION PLANS – (Continued)

A summary of the restricted stock activity under the Incentive Plan for the nine months ended September 30, 2012 and 2011 is presented below:

(In thousands)

Restricted Stock	Number of Shares For the Nine Months Ended September 30,	
	2012	2011
Outstanding Beginning Balance	48	112
Granted	199	9
Vested	(37 )	(63 )
Forfeited	(3 )	(7 )
Outstanding Ending Balance	207	51

The grant-date fair value per share is estimated to equal the market price of our common stock on the date of grant. In addition to the 190,000 shares of restricted stock granted to our Chief Executive Officer in 2012, we grant time-based shares of restricted stock annually to team members based on attaining certain individual and Company performance criteria as a part of our annual incentive compensation program. Based on the terms of individual restricted stock grant agreements, these time-based shares generally vest over a period of three to five years, based on continuous employment.

A summary of the restricted stock unit activity under the Incentive Plan for the nine months ended September 30, 2012 and 2011 is presented below:

(In thousands, except per share data)

Restricted Stock Units	Nonvested		Vested		Total
	Number of Restricted Stock Units	Weighted Average Grant-Date Fair Value Per Share	Number of Restricted Stock Units	Weighted Average Grant-Date Fair Value Per Share	Number of Restricted Stock Units
Outstanding as of December 31, 2011	348	\$ 24.06	428	\$ 22.14	776
Granted	313	106.32	–	–	313 (1)
Vested	(143)	21.48	143	21.48	–(2)
Forfeited	(8)	15.80	–	–	(8)
Outstanding as of September 30, 2012	510	\$ 75.43	571	\$ 21.97	1,081

(In thousands, except per share data)

Restricted Stock Units	Nonvested		Vested		Total
	Number of Restricted Stock Units	Weighted Average Grant-Date Fair Value Per Share	Number of Restricted Stock Units	Weighted Average Grant-Date Fair Value Per Share	Number of Restricted Stock Units
	521	\$ 19.99	270	\$ 22.94	791

Outstanding as of December 31, 2010						
Granted	25	58.54	–	–	25	(3)
Vested	(158)	20.99	158	20.99	–	(4)
Forfeited	(34)	20.50	–	–	–	(34)
Outstanding as of September 30, 2011						
	354	\$ 22.07	428	\$ 22.14	782	

- (1) The distribution date of vested restricted stock units is February 18, 2019 for 3 restricted stock units. For 310 restricted stock units, the vested restricted stock units will be distributed in equal installments on December 31, 2022, 2023, 2024, 2025 and 2026.
- (2) The distribution date of vested restricted stock units is February 22, 2014 for 60 restricted stock units, February 22, 2016 for 77 restricted stock units and February 22, 2017 for 6 restricted stock units.
- (3) The distribution date of vested restricted stock units is February 22, 2018 for 5 restricted stock units and February 18, 2019 for 20 restricted stock units.
- (4) The distribution date of vested restricted stock units is February 22, 2014 for 60 restricted stock units, February 22, 2016 for 90 restricted stock units and February 22, 2017 for 8 restricted stock units.

Each restricted stock unit represents and has a value equal to one share of common stock. The grant-date fair value per share is estimated to equal the market price of our common stock on the date of grant. In addition to the 310,000 restricted stock units granted to our Chief Executive Officer in 2012, we grant performance-based restricted stock units to team members as part of our long-term incentive compensation program. These restricted stock units will be earned over a five-year period based upon the compounded annual growth rate in our adjusted economic profit, a non-GAAP financial measure.

Table of Contents

## 12. STOCK-BASED COMPENSATION PLANS – (Concluded)

Stock compensation expense consists of the following:

(In thousands)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2012	2011	2012	2011
Restricted stock	\$ 1,101	\$ 113	\$ 2,370	\$ 493
Restricted stock units	2,944	251	6,231	1,063
Total	\$ 4,045	\$ 364	\$ 8,601	\$ 1,556

While the restricted stock units and shares of restricted stock are generally expected to vest in equal, annual installments over the corresponding requisite service periods of the grants, the related stock-based compensation expense is not recognized on a straight-line basis over the same periods. Each installment is accounted for as a separate award and as a result, the fair value of each installment is recognized as stock-based compensation expense on a straight-line basis over the related vesting period. The following table details how the expenses associated with restricted stock and restricted stock units, which are expected to be recognized over a weighted average period of 3.5 years, will be recorded assuming performance targets are achieved in the periods currently estimated:

(In thousands)

Year	Restricted Stock Units	Restricted Stock	Total Projected Expense
Remainder of 2012	\$ 2,294	\$ 913	\$ 3,207
2013	7,624	3,086	10,710
2014	5,263	2,350	7,613
2015	4,298	2,029	6,327
2016	3,639	1,862	5,501
Thereafter	7,060	8,722	15,782
Total	\$ 30,178	\$ 18,962	\$ 49,140

Table of Contents

13. LITIGATION AND CONTINGENT LIABILITIES

In the normal course of business and as a result of the customer-oriented nature of the industry in which we operate, industry participants are frequently subject to various customer claims and litigation seeking damages and statutory penalties. The claims allege, among other theories of liability, violations of state, federal and foreign truth-in-lending, credit availability, credit reporting, customer protection, warranty, debt collection, insurance and other customer-oriented laws and regulations, including claims seeking damages for physical and mental damages relating to our repossession and sale of the customer's vehicle and other debt collection activities. As the assignee of Consumer Loans originated by Dealers, we may also be named as a co-defendant in lawsuits filed by customers principally against Dealers. We may also have disputes and litigation with Dealers. The claims may allege, among other theories of liability, that we breached our dealer servicing agreement. Many of these cases are filed as purported class actions and seek damages in large dollar amounts. The following matters include current actions to which we are a party and updates to matters that were disclosed in our Annual Report on Form 10-K for the year ended December 31, 2011.

On December 3, 2010, we received a civil investigative demand from the Office of the Missouri Attorney General relating to our practices regarding collections from Missouri consumers who claim to have not received title from the Dealer at the time of their purchase. On January 24, 2011, we provided an initial response and on May 16, 2011, we filed a supplemental response. We cooperated with the Attorney General throughout the entire investigation, which the State confirms has been completed. We have reached an agreement in principle with the State of Missouri to enter into an assurance of voluntary compliance that resolves all possible claims by the State in relation to the subject of the civil investigative demand but which involves no admission of any violation or wrongdoing by the Company. We will continue to work with the Attorney General to finalize the terms of the settlement.

On November 22, 2011, an arbitration proceeding against us was commenced before the American Arbitration Association ("AAA") in Southfield, Michigan. The arbitration demand was brought by a Dealer and sought unspecified money damages for alleged breach of the dealer servicing agreement. The claimant purported to proceed on behalf of a putative class of similarly situated Dealers. On or about January 3, 2012, we filed an answer, denying the allegations in the demand and opposing claimant's attempt to proceed on a class-wide basis based on the terms of the parties' arbitration agreement, which does not authorize class-wide arbitration, and recent controlling Supreme Court authority. An arbitration panel was never appointed. On August 1, 2012, we received notice that the Dealer dismissed the proceeding against the Company.

On September 7, 2012, an arbitration proceeding against us was commenced before the AAA in Southfield, Michigan. The arbitration demand was brought by a group of six Dealers and sought unspecified money damages for claims relating to the dealer servicing agreements of these Dealers. We previously received an unfiled demand from five of these six Dealers alleging similar claims. On or about September 27, 2012, we filed an objection to the consolidation of these arbitration claims based on the terms of the parties' respective arbitration agreements, which do not authorize consolidated arbitration proceedings. On October 9, 2012, the AAA sustained our objection holding that the cases could only proceed on an individual basis. Plaintiffs failed to do so and the AAA deemed the matter not properly filed.

An adverse ultimate disposition in any action to which we are a party or otherwise subject could have a material adverse impact on our financial position, liquidity and results of operations.



Table of Contents

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

The following discussion and analysis should be read in conjunction with the consolidated financial statements and related notes included in Item 8 - Financial Statements and Supplementary Data, of our 2011 Annual Report on Form 10-K, as well as Item 1- Consolidated Financial Statements, of this Form 10-Q, which is incorporated herein by reference.

Overview

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

For the three months ended September 30, 2012, consolidated net income was \$53.0 million, or \$2.12 per diluted share, compared to \$50.0 million, or \$1.91 per diluted share, for the same period in 2011. For the nine months ended September 30, 2012, consolidated net income was \$159.8 million, or \$6.22 per diluted share, compared to \$138.0 million, or \$5.19 per diluted share, for the same period in 2011. The increase in consolidated net income for the three and nine months ended September 30, 2012 was primarily due to an increase in the size of our Loan portfolio.

Critical Success Factors

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

Access to Capital

Our strategy for accessing capital on acceptable terms needed to maintain and grow the business is to: (1) maintain consistent financial performance; (2) maintain modest financial leverage; and (3) maintain multiple funding sources. Our funded debt to equity ratio is 2.1:1 as of September 30, 2012. We currently utilize the following primary forms of debt financing: (1) a revolving secured line of credit; (2) Warehouse facilities; (3) Term ABS financings; and (4) Senior Notes.

Consumer Loan Performance

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

We use a statistical model to estimate the expected collection rate for each Consumer Loan at the time of assignment. We continue to evaluate the expected collection rate of each Consumer Loan subsequent to assignment. Our evaluation becomes more accurate as the Consumer Loans age, as we use actual performance data in our forecast. By comparing our current expected collection rate for each Consumer Loan with the rate we projected at the time of assignment, we are able to assess the accuracy of our initial forecast. The following table compares our forecast of Consumer Loan collection rates as of September 30, 2012, with the forecasts as of June 30, 2012, as of December 31, 2011, and at the time of assignment, segmented by year of assignment:

Consumer Loan Assignment Year	Forecasted Collection Percentage as of				Variance in Forecasted Collection Percentage from		
	September 30, 2012	June 30, 2012	December 31, 2011	Initial Forecast	June 30, 2012	December 31, 2011	Initial Forecast
2003	73.8%	73.8%	73.7%	72.0%	0.0%	0.1%	1.8%
2004	73.0%	73.0%	73.0%	73.0%	0.0%	0.0%	0.0%
2005	73.5%	73.6%	73.6%	74.0%	-0.1%	-0.1%	-0.5%
2006	70.0%	70.0%	70.0%	71.4%	0.0%	0.0%	-1.4%
2007	68.1%	68.1%	68.1%	70.7%	0.0%	0.0%	-2.6%
2008	70.3%	70.3%	70.0%	69.7%	0.0%	0.3%	0.6%
2009	79.5%	79.6%	79.4%	71.9%	-0.1%	0.1%	7.6%
2010	77.2%	77.1%	76.8%	73.6%	0.1%	0.4%	3.6%
2011	73.7%	73.6%	73.2%	72.5%	0.1%	0.5%	1.2%
2012 (1)	71.6%	71.9%	–	71.1%	-0.3%	–	0.5%

Table of Contents

(1) The forecasted collection rate for 2012 Consumer Loans as of September 30, 2012 includes both Consumer Loans that were in our portfolio as of June 30, 2012 and Consumer Loans assigned during the most recent quarter. The following table provides forecasted collection rates for each of these segments:

2012 Consumer Loan Assignment Period	Forecasted Collection Percentage as of		Variance
	September 30, 2012	June 30, 2012	
January 1, 2012 through June 30, 2012	72.0%	71.9%	0.1%
July 1, 2012 through September 30, 2012	70.6%	–	–

Consumer Loans assigned in 2003 and 2009 through 2011 have yielded forecasted collection results materially better than our initial estimates, while Consumer Loans assigned in 2006 and 2007 have yielded forecasted collection results materially worse than our initial estimates. For all other assignment years presented, actual results have been very close to our initial estimates. For the three months ended September 30, 2012, forecasted collection rates were generally consistent with expectations at the start of the period for all assignment years presented. For the nine months ended September 30, 2012, forecasted collection rates improved for Consumer Loans assigned during 2008 and 2010 through 2012 and were generally consistent with expectations at the start of the period for all other assignment years presented.

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

The following table presents forecasted Consumer Loan collection rates, advance rates, the spread (the forecasted collection rate less the advance rate), and the percentage of the forecasted collections that had been realized as of September 30, 2012. All amounts, unless otherwise noted, are presented as a percentage of the initial balance of the Consumer Loan (principal + interest). The table includes both Dealer Loans and Purchased Loans.

Consumer Loan Assignment Year	As of September 30, 2012			
	Forecasted Collection %	Advance % (1)	Spread %	% of Forecast Realized (2)
2003	73.8%	43.4%	30.4%	99.6%
2004	73.0%	44.0%	29.0%	99.5%
2005	73.5%	46.9%	26.6%	99.4%
2006	70.0%	46.6%	23.4%	98.8%
2007	68.1%	46.5%	21.6%	97.8%
2008	70.3%	44.6%	25.7%	96.1%
2009	79.5%	43.9%	35.6%	93.1%
2010	77.2%	44.7%	32.5%	73.8%
2011	73.7%	45.5%	28.2%	43.9%
2012	71.6%	45.9%	25.7%	13.5%

(1) Represents advances paid to Dealers on Consumer Loans assigned under our Portfolio Program and one-time payments made to Dealers to purchase Consumer Loans assigned under our Purchase Program as a percentage of the initial balance of the Consumer Loans. Payments of Dealer Holdback and accelerated Dealer Holdback are



not included.

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

The risk of a material change in our forecasted collection rate declines as the Consumer Loans age. For 2009 and prior Consumer Loan assignments, the risk of a material forecast variance is modest, as we have currently realized in excess of 90% of the expected collections. Conversely, the forecasted collection rates for more recent Consumer Loan assignments are less certain as a significant portion of our forecast has not been realized.

The spread between the forecasted collection rate and the advance rate declined during the 2004 through 2007 period as we increased advance rates during this period in response to a more difficult competitive environment. During 2008 and 2009, the spread increased as the competitive environment improved, and we reduced advance rates. In addition, during 2009, the spread was positively impacted by better than expected Consumer Loan performance. During the 2010 through 2012 period, the spread decreased as we again increased advance rates in response to the competitive environment.

Table of Contents

The following table presents forecasted Consumer Loan collection rates, advance rates, and the spread (the forecasted collection rate less the advance rate) as of September 30, 2012 for Dealer Loans and Purchased Loans separately. All amounts are presented as a percentage of the initial balance of the Consumer Loan (principal + interest).

Consumer Loan Assignment Year		Forecasted Collection %	Advance % (1)	Spread %
Dealer Loans	2007	68.0	% 45.8	% 22.2
	2008	70.8	% 43.3	% 27.5
	2009	79.6	% 43.5	% 36.1
	2010	77.2	% 44.4	% 32.8
	2011	73.7	% 45.4	% 28.3
	2012	71.6	% 45.5	% 26.1
Purchased Loans	2007	68.4	% 49.1	% 19.3
	2008	69.6	% 46.7	% 22.9
	2009	79.4	% 45.3	% 34.1
	2010	77.0	% 46.5	% 30.5
	2011	74.2	% 46.1	% 28.1
	2012	72.5	% 50.2	% 22.3

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

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

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

## Consumer Loan Volume

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

Three Months Ended	Year over Year Percent Change	
	Unit Volume	Dollar Volume (1)
March 31, 2011	36.7	% 59.3
June 30, 2011	28.7	% 41.3
September 30, 2011	28.6	% 40.5

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

December 31, 2011	25.3	%	32.1	%
March 31, 2012	10.6	%	10.7	%
June 30, 2012	7.3	%	7.9	%
September 30, 2012	5.4	%	3.1	%

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

Consumer Loan assignment volumes depend on a number of factors including (1) the overall demand for our product, (2) the amount of capital available to fund new Loans, and (3) our assessment of the volume that our infrastructure can support. Our pricing strategy is intended to maximize the amount of economic profit we generate, within the confines of capital and infrastructure constraints.

Unit and dollar volumes grew 5.4% and 3.1%, respectively, during the third quarter of 2012 as the number of active Dealers grew 26.6% and average volume per active Dealer declined 16.5%. We believe the decline in volume per Dealer is the result of increased competition. We increased advance rates in April 2012 and September 2012, which positively impacted unit and dollar volumes while reducing the return on capital we expect to earn on new assignments. We believe these advance rate increases had a positive impact on economic profit as we believe the positive impact of the increased dollar volume exceeded the negative impact of the reduced return on capital. Unit volume for the one month ended October 31, 2012 increased by 13.3% as compared to the same period in 2011 and was positively impacted by two additional business days (23 business days in October 2012 compared to 21 business days in October 2011).

Table of Contents

The following table summarizes the changes in Consumer Loan unit volume and active Dealers:

	For the Nine Months Ended September 30,		
	2012	2011	% Change
Consumer Loan unit volume	148,580	137,592	8.0%
Active Dealers (1)	4,781	3,603	32.7%
Average volume per active Dealer	31.1	38.2	-18.6%

(1) Active Dealers are Dealers who have received funding for at least one Loan during the period.

The following table provides additional information on the changes in Consumer Loan unit volume and active Dealers:

	For the Nine Months Ended September 30,			
	2012	2011	% Change	
Consumer Loan unit volume from Dealers active both periods	118,827	128,491	-7.5	%
Dealers active both periods	2,841	2,841	-	
Average volume per Dealers active both periods	41.8	45.2	-7.5	%
Consumer Loan unit volume from new Dealers	20,240	13,812	46.5	%
New active Dealers (1)	1,556	1,021	52.4	%
Average volume per new active Dealers	13.0	13.5	-3.7	%
Attrition (2)	-6.6	% -7.4	%	

(1) New active Dealers are Dealers who enrolled in our program and have received funding for their first Loan from us during the period.

(2) Attrition is measured according to the following formula: decrease in Consumer Loan unit volume from Dealers who have received funding for at least one Loan during the comparable period of the prior year but did not receive funding for any Loans during the current period divided by prior year comparable period Consumer Loan unit volume.

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

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2012	2011	2012	2011
Dealer Loan unit volume as a percentage of total unit volume	93.8%	92.3%	93.6%	92.4%
Dealer Loan dollar volume as a percentage of total dollar volume (1)	92.1%	90.1%	91.8%	90.4%

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

For the three and nine months ended September 30, 2012, Dealer Loan unit and dollar volume as a percentage of total unit and dollar volume were generally consistent with the same periods in 2011.

As of September 30, 2012 and December 31, 2011, the net Dealer Loans receivable balance was 87.7% and 85.4%, respectively, of the total net Loans receivable balance.

Table of Contents

## Results of Operations

Three Months Ended September 30, 2012 Compared to Three Months Ended September 30, 2011

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

(In thousands, except per share data)

	For the Three Months Ended September 30,		
	2012	2011	% Change
<b>Revenue:</b>			
Finance charges	\$ 137,495	\$ 117,905	16.6%
Premiums earned	12,206	10,462	16.7%
Other income	5,977	5,372	11.3%
Total revenue	155,678	133,739	16.4%
<b>Costs and expenses:</b>			
Salaries and wages	21,720	15,929	36.4%
General and administrative	6,797	6,044	12.5%
Sales and marketing	8,129	5,587	45.5%
Provision for credit losses	9,759	4,550	114.5%
Interest	16,289	14,600	11.6%
Provision for claims	9,122	8,363	9.1%
Total costs and expenses	71,816	55,073	30.4%
Income before provision for income taxes	83,862	78,666	6.6%
Provision for income taxes	30,874	28,706	7.6%
Net income	\$ 52,988	\$ 49,960	6.1%
<b>Net income per share:</b>			
Basic	\$ 2.13	\$ 1.92	
Diluted	\$ 2.12	\$ 1.91	
<b>Weighted average shares outstanding:</b>			
Basic	24,908	26,033	
Diluted	24,962	26,136	

Table of Contents

The following table highlights changes in net income for the three months ended September 30, 2012, as compared to 2011:

(In thousands)	Change
Net income for the three months ended September 30, 2011	\$ 49,960
Increase in finance charges	19,590
Increase in premiums earned	1,744
Increase in other income	605
Increase in operating expenses (1)	(9,086)
Increase in provision for credit losses	(5,209)
Increase in interest	(1,689)
Increase in provision for claims	(759)
Increase in provision for income taxes	(2,168)
Net income for the three months ended September 30, 2012	\$ 52,988

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

Finance Charges. For the three months ended September 30, 2012, finance charges increased \$19.6 million, or 16.6%, as compared to the same period in 2011. The increase was primarily the result of an increase in the average net Loans receivable balance partially offset by a decrease in the average yield on our Loan portfolio, as follows:

(Dollars in thousands)	For the Three Months Ended September		
	2012	30, 2011	Change
Average net Loans receivable balance	\$ 1,848,512	\$ 1,478,779	\$ 369,733
Average yield on our Loan portfolio	29.8%	31.9%	-2.1%

The following table summarizes the impact each component had on the overall increase in finance charges for the three months ended September 30, 2012:

(In thousands)	Year over Year Change For the Three Months Ended September 30, 2012
Impact on finance charges:	
Due to an increase in the average net Loans receivable balance	\$ 29,479
Due to a decrease in the average yield	(9,889)
Total increase in finance charges	\$ 19,590

The increase in the average net Loans receivable balance was primarily due to growth in new Loan volume during the last two quarters of 2011 and the first three quarters of 2012, which was primarily a result of an increase in active Dealers. The average yield on our Loan portfolio for the three months ended September 30, 2012 decreased as compared to the same period in 2011 due to lower yields on new Loans, partially offset by improvements in forecasted collection rates during the last two quarters of 2011 and the first two quarters of 2012.

Premiums Earned. For the three months ended September 30, 2012, premiums earned increased \$1.7 million, or 16.7%, as compared to the same period in 2011. The increase is primarily due to growth in the size of our reinsurance portfolio which resulted from growth in new Consumer Loan assignments during the last two quarters of 2011 and the first three quarters of 2012.

Other Income. For the three months ended September 30, 2012, other income increased \$0.6 million, or 11.3%, as compared to the same period in 2011. The increase is primarily due to an increase in Global Positioning Systems with Starter Interrupt Devices (“GPS-SID”) fee income due to increases in both the fee earned per unit and the number of units purchased by Dealers from third party providers.



Table of Contents

Operating Expenses. For the three months ended September 30, 2012, operating expenses increased \$9.1 million, or 33.0%, as compared to the same period in 2011. The change in operating expenses is primarily due to the following:

- An increase in salaries and wages expense of \$5.8 million, or 36.4%, which included a \$3.7 million increase in stock-based compensation expense primarily attributable to the 15 year stock award granted to our Chief Executive Officer during the first quarter of the year and a \$0.9 million increase in fringe benefits, primarily related to medical claims. Salaries and wages, excluding the increase in stock-based compensation and fringe benefits, increased \$1.2 million including an increase of \$0.9 million in loan servicing, \$0.2 million for support functions and \$0.1 million in loan originations.
- An increase in sales and marketing expense of \$2.5 million, or 45.5%, primarily as a result of the increase in the size of our field sales force.

Provision for Credit Losses. For the three months ended September 30, 2012, the provision for credit losses increased \$5.2 million, or 114.5%, as compared to the same period in 2011. Under GAAP, when the present value of forecasted future cash flows decline relative to our expectations at the time of assignment, a provision for credit losses is recorded immediately as a current period expense and a corresponding allowance for credit losses is established. For purposes of calculating the required allowance, Dealer Loans are grouped by Dealer and Purchased Loans are grouped by month of purchase. As a result, regardless of the overall performance of the portfolio of Consumer Loans, a provision can be required if any individual Loan pool performs worse than expected. Conversely, a previously recorded provision can be reversed if any previously impaired individual Loan pool experiences an improvement in performance.

During the three months ended September 30, 2012, overall Consumer Loan performance was generally consistent with our expectations at the start of the period. However, the performance of certain Loan pools declined from our expectations during the period, resulting in a provision for credit losses of \$9.8 million for the three months ended September 30, 2012, of which \$10.2 million related to Dealer Loans partially offset by a reversal of a provision of \$0.4 million related to Purchased Loans. During the three months ended September 30, 2011, overall Consumer Loan performance exceeded our expectations at the start of the period. However, the performance of certain Loan pools declined from our expectations during the period, resulting in a provision for credit losses of \$4.5 million for the three months ended September 30, 2011, of which \$4.7 million related to Dealer Loans partially offset by a reversal of a provision of \$0.2 million related to Purchased Loans.

Interest. For the three months ended September 30, 2012, interest expense increased \$1.7 million, or 11.6%, as compared to the same period in 2011. The following table shows interest expense, the average outstanding debt balance, and the average cost of debt for the three months ended September 30, 2012 and 2011:

(Dollars in thousands)	For the Three Months Ended September	
	2012	2011
Interest expense	\$ 16,289	\$ 14,600
Average outstanding debt balance	1,202,821	941,531
Average cost of debt	5.4%	6.2%

For the three months ended September 30, 2012, the increase in interest expense is primarily due to the increase in the average outstanding debt balance, partially offset by a decline in our average cost of debt. The average outstanding debt balance increased compared to the same period in 2011 due to the use of the debt proceeds to fund the growth in new Consumer Loan assignments and stock repurchases. The decline in our average cost of debt was primarily a

result of a change in the mix of our outstanding debt.

**Provision for Claims.** For the three months ended September 30, 2012, provision for claims increased \$0.8 million, or 9.1%, as compared to the same period in 2011. The increase was due to an increase in the size of our reinsurance portfolio partially offset by a decrease in claims paid per reinsured vehicle service contract.

**Provision for Income Taxes.** For the three months ended September 30, 2012, the effective tax rate of 36.8% was generally consistent with the effective tax rate of 36.5% in the same period in 2011.

Table of Contents

## Results of Operations

Nine Months Ended September 30, 2012 Compared to Nine Months Ended September 30, 2011

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

(In thousands, except per share data)

	For the Nine Months Ended September 30,		
	2012	2011	% Change
<b>Revenue:</b>			
Finance charges	\$ 397,563	\$ 338,238	17.5%
Premiums earned	34,987	29,195	19.8%
Other income	17,313	19,783	-12.5%
Total revenue	449,863	387,216	16.2%
<b>Costs and expenses:</b>			
Salaries and wages	61,530	47,402	29.8%
General and administrative	21,463	18,186	18.0%
Sales and marketing	23,478	17,768	32.1%
Provision for credit losses	17,716	22,394	-20.9%
Interest	47,150	42,173	11.8%
Provision for claims	26,704	22,733	17.5%
Total costs and expenses	198,041	170,656	16.0%
Income before provision for income taxes	251,822	216,560	16.3%
Provision for income taxes	91,983	78,565	17.1%
Net income	\$ 159,839	\$ 137,995	15.8%
<b>Net income per share:</b>			
Basic	\$ 6.24	\$ 5.23	
Diluted	\$ 6.22	\$ 5.19	
<b>Weighted average shares outstanding:</b>			
Basic	25,629	26,397	
Diluted	25,706	26,573	

Table of Contents

The following table highlights changes in net income for the nine months ended September 30, 2012, as compared to 2011:

(In thousands)	Change
Net income for the nine months ended September 30, 2011	\$ 137,995
Increase in finance charges	59,325
Increase in premiums earned	5,792
Decrease in other income	(2,470)
Increase in operating expenses (1)	(23,115)
Decrease in provision for credit losses	4,678
Increase in interest	(4,977)
Increase in provision for claims	(3,971)
Increase in provision for income taxes	(13,418)
Net income for the nine months ended September 30, 2012	\$ 159,839

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

Finance Charges. For the nine months ended September 30, 2012, finance charges increased \$59.3 million, or 17.5%, as compared to the same period in 2011. The increase was primarily the result of an increase in the average net Loans receivable balance partially offset by a decrease in the average yield on our Loan portfolio, as follows:

(Dollars in thousands)	For the Nine Months Ended September 30,		
	2012	2011	Change
Average net Loans receivable balance	\$ 1,759,025	\$ 1,378,784	\$ 380,241
Average yield on our Loan portfolio	30.1%	32.7%	-2.6%

The following table summarizes the impact each component had on the overall increase in finance charges for the nine months ended September 30, 2012:

(In thousands)	Year over Year Change For the Nine Months Ended September 30, 2012
Impact on finance charges:	
Due to an increase in the average net Loans receivable balance	\$ 93,279
Due to a decrease in the average yield	(33,954)
Total increase in finance charges	\$ 59,325

The increase in the average net Loans receivable balance was primarily due to growth in new Loan volume throughout 2011 and 2012, which was primarily a result of an increase in active Dealers. The average yield on our Loan portfolio for the nine months ended September 30, 2012 decreased as compared to the same period in 2011 due to lower yields on new Loans, partially offset by improvements in forecasted collection rates throughout 2011 and the first two quarters of 2012.

Premiums Earned. For the nine months ended September 30, 2012, premiums earned increased \$5.8 million, or 19.8%, as compared to the same period in 2011. The increase is primarily due to growth in the size of our reinsurance portfolio which resulted from growth in new Consumer Loan assignments throughout 2011 and 2012.

Other Income. For the nine months ended September 30, 2012, other income decreased \$2.5 million, or 12.5%, as compared to the same period in 2011. The decrease in other income was primarily due to a decrease in Guaranteed Asset Protection (“GAP”) profit sharing income from \$6.9 million in the first three quarters of 2011 to \$1.7 million in the first three quarters of 2012. The decrease is primarily the result of the change we made to our revenue recognition during the second quarter of 2011 to begin recognizing this income as earned over the life of the GAP contracts. As a result of this change, 2011 included both the recognition of the annual profit sharing payment for 2010 received during the first quarter of 2011 (\$3.7 million) and the recognition of future profit sharing payments earned during the first three quarters of 2011 (\$3.2 million). In addition, profit sharing payments earned during the first three quarters of 2012 (\$1.7 million) included a \$0.5 million reversal in the first quarter of previously recognized income resulting from a change in our profit sharing arrangement. The \$5.2 million decrease in GAP profit sharing was partially offset by a \$2.8 million increase in GPS-SID fee income due to increases in both the fee earned per unit and the number of units purchased by dealers.

Table of Contents

Operating Expenses. For the nine months ended September 30, 2012, operating expenses increased \$23.1 million, or 27.7%, as compared to the same period in 2011. The change in operating expenses is due to the following:

- An increase in salaries and wages expense of \$14.1 million, or 29.8%, which included a \$7.0 million increase in stock-based compensation expense primarily attributable to the 15 year stock award granted to our Chief Executive Officer during the first quarter of the year and a \$1.9 million increase in fringe benefits, primarily related to medical claims. Salaries and wages, excluding the increase in stock-based compensation and fringe benefits, increased \$5.2 million including an increase of \$3.2 million in loan servicing, \$1.6 million for support functions and \$0.4 million in loan originations.
- An increase in sales and marketing expenses of \$5.7 million, or 32.1%, primarily as a result of the increase in the size of the field sales force.
- An increase in general and administrative expenses of \$3.3 million, or 18.0%, primarily due to a \$1.3 million increase in information technology expenses, an increase in legal expenses of \$0.9 million and \$0.9 million in higher taxes primarily as a result of a property tax refund recognized in the first quarter of 2011.

Provision for Credit Losses. For the nine months ended September 30, 2012, the provision for credit losses decreased \$4.7 million, or 20.9%, as compared to the same period in 2011. During the nine months ended September 30, 2012, overall Consumer Loan performance exceeded our expectations at the start of the period. However, the performance of certain Loan pools declined from our expectations during the period, resulting in a provision for credit losses of \$17.7 million for the nine months ended September 30, 2012, of which \$20.4 million related to Dealer Loans partially offset by a reversal of a provision of \$2.7 million related to Purchased Loans. During the nine months ended September 30, 2011, overall Consumer Loan performance exceeded our expectations at the start of the period. However, the performance of certain Loan pools declined from our expectations during the period, resulting in a provision for credit losses of \$22.4 million for the nine months ended September 30, 2011, of which \$23.0 million related to Dealer Loans offset by a reversal of provision of \$0.6 million related to Purchased Loans.

Interest. For the nine months ended September 30, 2012, interest expense increased \$5.0 million, or 11.8%, as compared to the same period in 2011. The following table shows interest expense, the average outstanding debt balance, and the average cost of debt for the nine months ended September 30, 2012 and 2011:

(Dollars in thousands)	For the Nine Months Ended September	
	2012	2011
Interest expense	\$ 47,150	\$ 42,173
Average outstanding debt balance	1,120,146	861,155
Average cost of debt	5.6%	6.5%

For the nine months ended September 30, 2012, the increase in interest expense is primarily due to the increase in the average outstanding debt balance, partially offset by a decline in our average cost of debt. The average outstanding debt balance increased compared to the same period in 2011 due to the use of the debt proceeds to fund the growth in new Consumer Loan assignments and stock repurchases. The decline in our average cost of debt was primarily a result of a change in the mix of our outstanding debt.

Provision for Claims. For the nine months ended September 30, 2012, provision for claims increased \$4.0 million, or 17.5%, as compared to the same period in 2011. The increase was due to an increase in the size of our reinsurance portfolio partially offset by a decrease in claims paid per reinsured vehicle service contract.

Provision for Income Taxes. For the nine months ended September 30, 2012, the effective tax rate of 36.5% was generally consistent with the effective tax rate of 36.3% in the same period in 2011.

Table of Contents

## Liquidity and Capital Resources

We need capital to maintain and grow our business. Our primary sources of capital are cash flows from operating activities, collections of Consumer Loans and borrowings under: (1) a revolving secured line of credit; (2) Warehouse facilities; (3) Term ABS financings; and (4) Senior Notes. There are various restrictive debt covenants for each financing arrangement and we are in compliance with those covenants as of September 30, 2012. For information regarding these financings and the covenants included in the related documents, see Note 5 to the consolidated financial statements contained in Item 1 of this Form 10-Q, which is incorporated herein by reference.

During the third quarter of 2012, we completed a \$252.0 million Term ABS financing which was used to repay outstanding indebtedness. The financing has an expected annualized cost of approximately 2.0% (including the initial purchaser's fees and other costs) and it will revolve for 24 months after which it will amortize based upon the cash flows on the contributed loans.

During the second quarter of 2012, we extended the maturity of our revolving secured line of credit facility from June 22, 2014 to June 22, 2015. Additionally, the amount of the facility was increased from \$205.0 million to \$235.0 million. The interest rate on borrowings under the facility was decreased from the prime rate plus 1.25% or the LIBOR rate plus 2.25%, at our option, to the prime rate plus 0.875% or the LIBOR rate plus 1.875%, at our option.

During the second quarter of 2012, we extended the date on which Warehouse III will cease to revolve from September 10, 2013 to September 10, 2015. The maturity of the facility was also extended from September 10, 2014 to September 10, 2017. There were no other material changes to the terms of the facility.

During the second quarter of 2012, we commenced a tender offer to repurchase 1.0 million shares of our common stock at a price of \$84.45 per share. Upon expiration of the tender offer during the second quarter of 2012, we repurchased 1.0 million common shares at a cost of \$84.5 million. The settlement during the third quarter of 2012 was financed by borrowing under our revolving secured line of credit facility.

During the first quarter of 2012, we completed a \$201.3 million Term ABS financing which was used to repay outstanding indebtedness. The financing has an expected annualized cost of approximately 2.8% (including the initial purchaser's fees and other costs) and it will revolve for 24 months after which it will amortize based upon the cash flows on the contributed loans.

Cash and cash equivalents as of September 30, 2012 and December 31, 2011 was \$5.7 million and \$4.7 million, respectively. Our total balance sheet indebtedness increased \$264.3 million to \$1,262.1 million as of September 30, 2012 from \$997.8 million as of December 31, 2011 due to the growth in new Consumer Loan assignments and stock repurchases.

## Contractual Obligations

A summary of our scheduled principal debt maturities as of September 30, 2012 is as follows:

(In thousands)

Year	Scheduled Principal Debt Maturities (1)
Remainder of 2012	\$ 23,849
2013	146,594
2014	443,207



2015		298,104
2016		—
Thereafter		350,000
Total	\$	1,261,754

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

The amounts presented exclude the net unamortized debt premium of \$0.3 million.

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

Table of Contents

Critical Accounting Estimates

Our consolidated financial statements are prepared in accordance with GAAP. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. On an ongoing basis, we review our accounting policies, assumptions, estimates and judgments to ensure that our financial statements are presented fairly and in accordance with GAAP. Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2011 discusses several critical accounting estimates, which we believe involve a high degree of judgment and complexity. There have been no material changes to the estimates and assumptions associated with these accounting estimates from those discussed in our Annual Report on Form 10-K for the year ended December 31, 2011.

Off-Balance Sheet Arrangements

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

Table of Contents

Forward-Looking Statements

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

We claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995 for all of our forward-looking statements. These forward-looking statements represent our outlook only as of the date of this report. While we believe that our forward-looking statements are reasonable, actual results could differ materially since the statements are based on our current expectations, which are subject to risks and uncertainties. Factors that might cause such a difference include, but are not limited to, the factors set forth in Item 1A of our Form 10-K for the year ended December 31, 2011, as amended in Item 1A of Part II of our Form 10-Q for the quarter ended June 30, 2012, as amended in Item 1A of Part II of this report, other risk factors discussed herein or listed from time to time in our reports filed with the SEC and the following:

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

- We may incur substantially more debt and other liabilities. This could exacerbate further the risks associated with our current debt levels.
- The regulation to which we are or may become subject could result in a material adverse effect on our business.
- Adverse changes in economic conditions, the automobile or finance industries, or the non-prime consumer market could adversely affect our financial position, liquidity and results of operations, the ability of key vendors that we depend on to supply us with services, and our ability to enter into future financing transactions.
- Litigation we are involved in from time to time may adversely affect our financial condition, results of operations and cash flows.
- Changes in tax laws and the resolution of uncertain income tax matters could have a material adverse effect on our results of operations and cash flows from operations.

Table of Contents

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

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

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Refer to our Annual Report on Form 10-K for the year ended December 31, 2011 for a complete discussion of our market risk. There have been no material changes to the market risk information included in our 2011 Annual Report on Form 10-K.

ITEM 4. CONTROLS AND PROCEDURES.

Evaluation of disclosure controls and procedures.

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

to allow timely decisions regarding required disclosure.

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

Table of Contents

PART II. - OTHER INFORMATION

ITEM 1A. RISK FACTORS

The risk factors entitled “Our operations are dependent on technology” and “Failure to properly safeguard confidential consumer information could subject us to liability, decrease our profitability and damage our reputation” included in Item 1A — “Risk Factors” of our Annual Report on Form 10-K for the year ended December 31, 2011 are amended and restated in their entirety as follows:

Failure to properly safeguard confidential consumer information could subject us to liability, decrease our profitability and damage our reputation.

In the ordinary course of our business, we collect, share and store sensitive data, including our proprietary business information and personally identifiable information of our customers and employees, on our computer networks. The secure processing, maintenance and transmission of this information is critical to our operations and business strategy.

If third parties or our team members are able to breach our network security, the network security of a third party that we share information with or otherwise misappropriate our customers’ personal financial information, or if we give third parties or our team members improper access to our customers’ personal financial information, we could be subject to liability. This liability could include identity theft or other similar fraud-related claims. This liability could also include claims for other misuses or losses of personal financial information, including for unauthorized marketing purposes. Other liabilities could include claims alleging misrepresentation of our privacy and data security practices.

We rely on encryption and authentication technology licensed from third parties to provide the security and authentication necessary to secure online transmission of confidential consumer information. Advances in computer capabilities, new discoveries in the field of cryptography or other events or developments may result in a compromise or breach of the algorithms that we use to protect sensitive customer transaction data. A party who is able to circumvent our security measures could misappropriate proprietary information or cause interruptions in our operations. We may be required to expend capital and other resources to protect against, or alleviate problems caused by, security breaches or other cybersecurity incidents. Although we have experienced cybersecurity incidents from time to time that have not had a material effect on our business, financial condition or results of operations, there can be no assurance that a cyber attack, security breach or other cybersecurity incident will not have a material adverse effect on us in the future. Our security measures are designed to protect against security breaches, but our failure to prevent security breaches could subject us to liability, decrease our profitability and damage our reputation.

ITEM 6. EXHIBITS

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

Table of Contents

SIGNATURE

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

CREDIT ACCEPTANCE CORPORATION  
(Registrant)

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

Date: November 1, 2012



Table of Contents

## INDEX OF EXHIBITS

The following documents are filed as part of this report. Those exhibits previously filed and incorporated herein by reference are identified below. Exhibits not required for this report have been omitted. Unless otherwise noted, the Company's commission file number for all exhibits incorporated by reference herein is 000-20202.

Exhibit No.	Description
4.75	Indenture dated as of September 20, 2012, between Credit Acceptance Auto Loan Trust 2012-2 and Wells Fargo Bank, National Association (incorporated by reference to an exhibit to the Company's Current Report on Form 8-K, dated September 20, 2012)
4.76	Sale and Servicing Agreement dated as of September 20, 2012, among the Company, Credit Acceptance Auto Loan Trust 2012-2, Credit Acceptance Funding LLC 2012-2, and Wells Fargo Bank, National Association (incorporated by reference to an exhibit to the Company's Current Report on Form 8-K, dated September 20, 2012)
4.77	Backup Servicing Agreement dated as of September 20, 2012, among the Company, Credit Acceptance Funding LLC 2012-2, Credit Acceptance Auto Loan Trust 2012-2, and Wells Fargo Bank, National Association (incorporated by reference to an exhibit to the Company's Current Report on Form 8-K, dated September 20, 2012)
4.78	Amended and Restated Trust Agreement dated as of September 20, 2012, between Credit Acceptance Funding LLC 2012-2 and U.S. Bank Trust National Association (incorporated by reference to an exhibit to the Company's Current Report on Form 8-K, dated September 20, 2012)
4.79	Sale and Contribution Agreement dated as of September 20, 2012, between the Company and Credit Acceptance Funding LLC 2012-2 (incorporated by reference to an exhibit to the Company's Current Report on Form 8-K, dated September 20, 2012)
4.80	Amended and Restated Intercreditor Agreement dated September 20, 2012, among the Company, CAC Warehouse Funding Corporation II, CAC Warehouse Funding III, LLC, CAC Warehouse Funding LLC IV, Credit Acceptance Funding LLC 2012-2, Credit Acceptance Funding LLC 2012-1, Credit Acceptance Funding LLC 2011-1, Credit Acceptance Funding LLC 2010-1, Credit Acceptance Auto Loan Trust 2012-2, Credit Acceptance Auto Loan Trust 2012-1, Credit Acceptance Auto Loan Trust 2011-1, Credit Acceptance Auto Loan Trust 2010-1, Fifth Third Bank, as agent, Wells Fargo Bank, National Association, as agent, Bank of Montreal, as agent and Comerica Bank, as agent (incorporated by reference to an exhibit to the Company's Current Report on Form 8-K, dated September 20, 2012)
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101(INS)	XBRL Instance Document. *
101(SCH)	XBRL Taxonomy Extension Schema Document. *
101(CAL)	XBRL Taxonomy Extension Calculation Linkbase Document. *
101(DEF)	XBRL Taxonomy Extension Definition Linkbase Document. *
101(LAB)	XBRL Taxonomy Extension Label Linkbase Document. *
101(PRE)	XBRL Taxonomy Extension Presentation Linkbase Document. *

\*Users of this data are advised pursuant to Rule 406T of Regulation S-T that this interactive data file is deemed not filed or part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, and otherwise is not subject to liability under these sections.

