CONSUMER PORTFOLIO SERVICES INC
Form 10-Q
April 24, 2012

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2012

Commission file number: 1-11416

CONSUMER PORTFOLIO SERVICES, INC.
(Exact name of registrant as specified in its charter)

California (State or other jurisdiction of incorporation or organization)	33-0459135 (IRS Employer Identification No.)
19500 Jamboree Road, Irvine, California (Address of principal executive offices)	92612 (Zip Code)

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

Former name, former address and former fiscal year, if changed since last report: N/A
Indicate by check mark whether the registrant (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes [X] No [ ]

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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 [x] No [ ]

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

Large Accelerated Filer [ ] Accelerated Filer [ ]
Non-Accelerated Filer [ ] Smaller Reporting Company [X]

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

As of April 10, 2012 the registrant had 19,331,257 common shares outstanding.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES
INDEX TO FORM 10-Q
For the Quarterly Period Ended March 31, 2012

Item 1. Financial Statements

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share and per share data)

	March 31, 2012	December 31, 2011
ASSETS		
Cash and cash equivalents	$10,614	$10,094
Restricted cash and equivalents	131,543	159,228
Finance receivables	554,999	516,630
Less: Allowance for finance credit losses	(11,251)	(10,351)
Finance receivables, net	543,748	506,279
Finance receivables measured at fair value	126,923	160,253
Residual interest in securitizations	4,612	4,414
Furniture and equipment, net	753	875
Deferred financing costs	9,099	8,036
Deferred tax assets, net	15,000	15,000
Accrued interest receivable	6,380	6,432
Other assets	18,655	19,439
	$867,327	$890,050
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities		
Accounts payable and accrued expenses	$25,955	$27,993
Warehouse lines of credit	28,929	25,393
Residual interest financing	18,015	21,884
Debt secured by receivables measured at fair value	133,017	166,828
Securitization trust debt	599,678	583,065
Senior secured debt, related party	53,570	58,344
Subordinated renewable notes	20,741	20,750
	879,905	904,257
COMMITMENTS AND CONTINGENCIES		
Shareholders' Equity		
Preferred stock, $1 par value; authorized 5,000,000 shares; none issued	-	-
Series A preferred stock, $1 par value; authorized 5,000,000 shares; none issued	-	-
Series B convertible preferred stock, $1 par value; authorized 1,870 shares; none issued and outstanding at March 31, 2012 and December 31, 2011, respectively	-	-
Common stock, no par value; authorized 75,000,000 shares; 19,331,257 and 19,526,968 shares issued and outstanding at March 31, 2012 and December 31, 2011, respectively	63,583	62,466
Accumulated deficit	(67,626)	(68,138)

Accumulated other comprehensive loss	(8,535)	(8,535)
	(12,578)	(14,207)
	$867,327	$890,050

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

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

	Three Months Ended March 31,	
	2012	2011
Revenues:		
Interest income	$40,611	$28,584
Servicing fees	801	1,415
Other income	3,106	2,396
	44,518	32,395
Expenses:		
Employee costs	8,871	7,623
General and administrative	4,497	3,639
Interest	22,309	19,126
Provision for credit losses	4,836	3,692
Marketing	2,620	1,596
Occupancy	721	761
Depreciation and amortization	152	164
	44,006	36,601
Income (loss) before income tax expense	512	(4,206)
Income tax expense	-	-
Net income (loss)	$512	$(4,206)
Income (loss) per share:		
Basic	$0.03	$(0.23)
Diluted	0.02	(0.23)
Number of shares used in computing income (loss) per share:		
Basic	19,416	18,122
Diluted	22,601	18,122

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(In thousands)

	Three Months Ended March 31	
	2012	2011
Net income/(loss)	$512	$(4,206)
Other comprehensive income/(loss); change in funded status of pension plan	-	-
Comprehensive income/(loss)	$512	$(4,206)

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

	Three Months Ended March 31, 2012	Three Months Ended March 31, 2011
Cash flows from operating activities:		
Net income (loss)	$512	$(4,206)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Accretion of deferred acquisition fees	(3,335)	(1,999)
Accretion of purchase discount on receivables measured at fair value	(4,163)	--
Amortization of discount on securitization notes	592	949
Amortization of discount on senior secured debt, related party	826	610
Accretion of premium on debt secured by receivables measured at fair value	2,980	--
Mark to fair value on debt secured by receivables measured at fair value	2,400	--
Mark to fair value of receivables measured at fair value	(1,510)	--
Depreciation and amortization	152	164
Amortization of deferred financing costs	1,477	1,109
Provision for credit losses	4,836	3,692
Stock-based compensation expense	293	371
Interest income on residual assets	(198)	(144)
Changes in assets and liabilities:		
Accrued interest receivable	52	886
Other assets	526	925
Accounts payable and accrued expenses	(982)	1,123
Net cash provided by operating activities	4,458	3,480
Cash flows from investing activities:		
Purchases of finance receivables held for investment	(119,902)	(50,036)
Proceeds received on finance receivables held for investment	119,935	93,830
Change in repossessions in inventory	258	(1,754)
Decreases (Increases) in restricted cash and equivalents	27,685	(7,164)
Purchase of furniture and equipment	(30)	(20)
Net cash provided by investing activities	27,946	34,856
Cash flows from financing activities:		
Proceeds from issuance of securitization trust debt	155,000	--
Proceeds from issuance of subordinated renewable notes	638	375
Proceeds from issuance of senior secured debt, related party	-	4,660
Payments on subordinated renewable notes	(647)	(503)
Net proceeds from (repayments to) warehouse lines of credit	3,536	35,462
Proceeds from (repayments of) residual interest financing debt	(3,869)	(4,616)
Repayment of securitization trust debt	(138,979)	(79,406)
Repayment of portfolio acquisition facility	(39,191)	-
Repayment of senior secured debt, related party	(5,600)	-
Payment of financing costs	(2,540)	(1,325)
Repurchase of common stock	(244)	(8)

Exercises of options and warrants	12	-
Net cash provided by (used in) financing activities	(31,884)	(45,361)
Increase (decrease) in cash and cash equivalents	520	(7,025)
Cash and cash equivalents at beginning of period	10,094	16,252
Cash and cash equivalents at end of period	$10,614	$9,227
Supplemental disclosure of cash flow information:		
Cash paid (received) during the period for:		
Interest	$22,181	$16,290
Income taxes	$147	$-
Non-cash financing activities:		
Derivative warrants reclassified from liabilities to common stock upon amendment	$1,056	$--

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

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

(1) Summary of Significant Accounting Policies

Description of Business

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

Basis of Presentation

Our Unaudited Condensed Consolidated Financial Statements have been prepared in conformity with accounting principles generally accepted in the United States of America, with the instructions to Form 10-Q and with Article 8 of Regulation S-X of the Securities and Exchange Commission, and include all adjustments that are, in management's opinion, necessary for a fair presentation of the results for the interim periods presented. All such adjustments are, in the opinion of management, of a normal recurring nature. In addition, certain items in prior period financial statements may have been reclassified for comparability to current period presentation. Results for the three-month period ended March 31, 2012 are not necessarily indicative of the operating results to be expected for the full year.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted from these Unaudited Condensed Consolidated Financial Statements. These Unaudited Condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and Notes to Consolidated Financial Statements included in our Annual Report on Form 10-K for the year ended December 31, 2011.

Use of Estimates

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

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

Other Income

The following table presents the primary components of Other Income:

	March 31, 2012	March 31, 2011
	(In thousands)	
Direct mail revenues	$ 1,619	$ 1,168
Convenience fee revenue	832	714
Recoveries on previously charged-off contracts	97	187
Sales tax refunds	72	149
Other	486	178
Other income for the period	$ 3,106	$ 2,396

Stock-based Compensation

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

For the three months ended March 31, 2012 and 2011, we recorded stock-based compensation costs in the amount of $293,000 and $371,000, respectively. As of March 31, 2012, unrecognized stock-based compensation costs to be recognized over future periods equaled $1.7 million. This amount will be recognized as expense over a weighted-average period of 2.5 years.

The following represents stock option activity for the three months ended March 31, 2012:

	Number of Shares (in thousands)	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term
Options outstanding at the beginning of period…………	8,431	$ 1.53	N/A
Granted………………………………………………	-	-	N/A
Exercised…………………...……………………	(15)	0.77	N/A
Forfeited…………………………………………	(245)	1.39	N/A
Options outstanding at the end of period……………..…	8,171	$ 1.54	5.86 years
Options exercisable at the end of period…………..……	5,037	$ 1.72	4.17 years

At March 31, 2012, the aggregate intrinsic value of options outstanding and exercisable was $876,000 and $309,000, respectively. There were 15,000 shares exercised for the three months ended March 31, 2012 compared to 3,000 for the comparable period in 2011. There were 823,000 shares available for future stock option grants under existing plans as of March 31, 2012.

Purchases of Company Stock

During the three-month periods ended March 31, 2012 and 2011, we purchased 227,298 and 6,000 shares, respectively, of our common stock, at average prices of $1.15 and $1.34, respectively.

Reclassifications

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

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

Derivative Financial Instruments

We do not use derivative financial instruments to hedge exposures to cash-flow or market risks. However, from 2008 to 2010, we issued warrants to purchase the Company's common stock in conjunction with various debt financing transactions. At the time of issuance, four of these warrants issued contained "down round" or reset features that are subject to classification as liabilities for financial statement purposes. These liabilities are measured at fair value, with the changes in fair value at the end of each period reflected as current period income or loss. Accordingly, changes to the market price per share of our common stock underlying these warrants with "down round" or price reset features directly affect the fair value computations for these derivative financial instruments. The effect is that any increase in the market price per share of our common stock also increases the related liability, which in turn would result in a current period loss. Conversely, any decrease in the market price per share of our common stock also decreases the related liability, which in turn would result in a current period gain. We use a binomial pricing model to compute the fair value of the liabilities associated with the outstanding warrants. In computing the fair value of the warrant liabilities at the end of each period, we use significant judgments with respect to the risk free interest rate, the volatility of our stock price, and the estimated life of the warrants. The effects of these judgments, if proven incorrect, could have a significant effect on our financial statements. The warrant liabilities are included in Accounts payable and accrued expenses on our consolidated balance sheets. On March 29, 2012 we amended three of the four warrants that contained the "down round" features to remove those specific price reset terms. On the date of the amendment, we valued each of the three warrants using a binomial pricing model as described above. The aggregate value of the three amended warrants of $1.1 million was then reclassified from Accounts payable to Common Stock. The remaining warrant with the "down round" feature was not amended and was valued and recorded at March 31, 2012 using a binomial pricing model to compute the fair value, which is included in Accounts payable and accrued expenses, and will continue to be subject to quartely valuations.

Financial Covenants

Certain of our securitization transactions, our warehouse credit facilities and our residual interest financing contain various financial covenants requiring minimum financial ratios and results. Such covenants include maintaining minimum levels of liquidity and net worth and not exceeding maximum leverage levels. As of March 31, 2012, we were in compliance with all such covenants. In addition, certain securitization and non-securitization related debt agreements contain cross-default provisions that would allow certain creditors to declare a default if a default occurred under a different facility.

Finance Receivables and Related Debt Measured at Fair Value

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

(2) Finance Receivables

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

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

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

Finance Receivables	March 31, 2012	December 31, 2011
	(In thousands)	
Automobile finance receivables, net of unearned interest	$579,745	$536,773
Less: Unearned acquisition fees and originations costs	(24,746)	(20,143)
Finance Receivables	$554,999	$516,630

We consider an automobile contract delinquent when an obligor fails to make at least 90% of a contractually due payment by the following due date, which date may have been extended within limits specified in the servicing agreements. The period of delinquency is based on the number of days payments are contractually past due. Automobile contracts less than 31 days delinquent are not included. The period of delinquency is based on the number of days a payment is past its due date, as extended where applicable. In certain circumstances we will grant obligors one-month payment extensions to assist them with temporary cash flow problems. The only modification of terms is to advance the obligor's next due date by one month and extend the maturity date of the receivable by one month. In some cases, a two-month extension may be granted. There are no other concessions such as a reduction in interest rate, forgiveness of principal or of accrued interest. Accordingly, we consider such extensions to be insignificant delays in payments rather than troubled debt restructurings. The following table summarizes the delinquency status of finance receivables as of March 31, 2012 and December 31, 2011:

	March 31, 2012	December 31, 2011
	(In thousands)	
Deliquency Status		
Current	$ 566,583	$ 512,802
31 - 60 days	5,962	9,344
61 - 90 days	3,823	6,034
91 + days	3,377	8,593
	$ 579,745	$ 536,773

Finance receivables totaling $3.4 million and $13.0 million at March 31, 2012 and December 31, 2011, respectively, including all receivables greater than 90 days delinquent have been placed on non-accrual status as a result of their delinquency status.

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

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

The following table presents a summary of the activity for the allowance for credit losses for the three-month periods ended March 31, 2012 and 2011:

	Three Months Ended March 31,	
	2012	2011
	(In thousands)	
Balance at beginning of period	$ 10,351	$ 13,168
Provision for credit losses on finance receivables	4,836	3,692
Charge-offs	(8,302)	(9,902)
Recoveries	4,366	4,641
Balance at end of period	$ 11,251	$ 11,599

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

	March 31, 2012	December 31, 2011
	(In thousands)	
Gross balance of repossessions in inventory	$ 8,680	$ 9,246
Allowance for losses on repossessed inventory	(4,170)	(4,765)
Net repossessed inventory included in other assets	$ 4,510	$ 4,481

(3) Finance Receivables Measured at Fair Value

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

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

	March 31, 2012	December 31, 2011
Finance Receivables Measured at Fair Value	(In thousands)	
Finance receivables and accrued interest, net of unearned interest	$ 133,169	$ 172,167
Less: Fair value adjustment	(6,246)	(11,914)
Finance receivables measured at fair value	$ 126,923	$ 160,253

The following table summarizes the delinquency status of finance receivables measured at fair value as of March 31, 2012 and December 31, 2011:

	March 31, 2012	December 31, 2011
	(In thousands)	
Deliquency Status		
Current	$ 130,226	$ 164,625
31 - 60 days	1,675	4,872
61 - 90 days	782	1,767
91 + days	486	903
	$ 133,169	$ 172,167

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

(4) Securitization Trust Debt

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

Series	Final Scheduled Payment Date (1)	Receivables Pledged at March 31, 2012	Initial Principal	Outstanding Principal at March 31, 2012	Outstanding Principal at December 31, 2011	Weighted Average Contractual Interest Rate at March 31, 2012
			(Dollars in thousands)			
CPS 2006-B	January 2013	$ -	$ 257,500	$ -	$ 6,604	-
CPS 2006-C	June 2013	-	247,500	-	14,873	-
CPS 2006-D	August 2013	-	220,000	-	15,716	-
CPS 2007-A	November 2013	-	290,000	-	34,312	-
CPS 2007-TFC	December 2013	-	113,293	-	7,771	-
CPS 2007-B	January 2014	24,845	314,999	32,272	40,916	6.77%
CPS 2007-C	May 2014	33,711	327,499	41,998	52,723	6.91%
CPS 2008-A	October 2014	43,829	310,359	64,133	77,284	8.37%
Page Five Funding	January 2018	33,994	9,174	33,115	36,701	9.46%
CPS 2011-A	April 2018	73,865	100,364	69,175	75,625	3.95%
CPS 2011-B	September 2018	97,553	109,936	92,492	101,268	4.40%
CPS 2011-C	March 2019	113,916	119,400	111,511	119,272	4.85%
CPS 2012-A	June 2019	103,425	155,000	154,982	-	3.33%
		$ 525,138	$ 2,575,024	$ 599,678	$ 583,065	

(1) The Final Scheduled Payment Date represents final legal maturity of the securitization trust debt. Securitization trust debt is expected to become due and to be paid prior to those dates, based on amortization of the finance receivables pledged to the Trusts. Expected payments, which will depend on the performance of such receivables, as to which there can be no assurance, are $178.4 million in 2012, $171.3 million in 2013, $110.5 million in 2014, $81.8 million in 2015, $41.6 million in 2016 and $16.1 million in 2017.

All of the securitization trust debt was sold in private placement transactions to qualified institutional buyers. The debt was issued through our wholly-owned bankruptcy remote subsidiaries and is secured by the assets of such subsidiaries, but not by our other assets. Principal of $90.8 million, and the related interest payments, are guaranteed by financial guaranty insurance policies issued by third party financial institutions.

The terms of the various securitization agreements related to the issuance of the securitization trust debt andthe warehouse credit facilities require that we meet certain delinquency and credit loss criteria with respect to the collateral pool, and certain of the agreements require that we maintain minimum levels of liquidity and net worth and not exceed maximum leverage levels. In addition, certain securitization and non-securitization related debt contain cross-default provisions, which would allow certain creditors to declare a default if a default were declared under a different facility.

We are responsible for the administration and collection of the automobile contracts. The securitization agreements also require certain funds be held in restricted cash accounts to provide additional collateral for the borrowings or to be applied to make payments on the securitization trust debt. As of March 31, 2012, restricted cash under the various agreements totaled approximately $131.5 million. Interest expense on the securitization trust debt consists of the stated rate of interest plus amortization of additional costs of borrowing. Additional costs of borrowing include facility fees, insurance and amortization of deferred financing costs and discounts on notes sold. Deferred financing costs and discounts on notes sold related to the securitization trust debt are amortized using a level yield method. Accordingly, the effective cost of the securitization trust debt is greater than the contractual rate of interest disclosed above.

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

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

(5) Debt

The terms and amounts of our other debt outstanding at March 31, 2012 and December 31, 2011 are summarized below:

			Amount Outstanding at	
			March 31, 2012	December 31, 2011
			(In thousands)	
Description	Interest Rate	Maturity		
Residual interest financing	12.875% over one month Libor	February 2013	$ 18,015	$ 21,884
Senior secured debt, related party	14.00%	February 2012	-	5,000
	14.00%	June 2012	600	1,200
	14.00%	October 2012	5,000	5,000
	16.00%	December 2013	47,970	47,144
Subordinated renewable notes	Weighted average rate of 14.6% and 14.6% at March 31, 2012 and December 31, 2011, respectively	Weighted average maturity of January 2014 and August 2014 at March 31, 2012 and December 31, 2011, respectively	20,741	20,750
			$ 92,326	$ 100,978

(6) Interest Income and Interest Expense

The following table presents the components of interest income:

	Three Months Ended
	March 31,

	2012	2011
	(In thousands)	
Interest on Finance Receivables	$ 40,145	$ 28,164
Residual interest income	224	195
Other interest income	242	225
Interest income	$ 40,611	$ 28,584

The following table presents the components of interest expense:

	Three Months Ended March 31,	
	2012	2011
	(In thousands)	
Securitization trust debt	$ 10,020	$ 12,004
Warehouse debt	1,396	2,344
Senior secured debt, related party	3,537	2,667
Debt secured by receivables at fair value	5,790	-
Residual interest debt	748	1,342
Subordinated debt	818	769
Interest Expense	$ 22,309	$ 19,126

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(7) Earnings (Loss) Per Share

Earnings (loss) per share for the three-month periods ended March 31, 2012 and 2011 were calculated using the weighted average number of shares outstanding for the related period. The following table reconciles the number of shares used in the computations of basic and diluted earnings (loss) per share for the three-month periods ended March 31, 2012 and 2011:

	Three Months Ended March 31,	
	2012	2011
	(In thousands)	
Weighted average number of common shares outstanding during the period used to compute basic earnings (loss) per share	19,416	18,122
Incremental common shares attributable to exercise of outstanding options and warrants	3,185	-
		21,528
Weighted average number of common shares used to compute diluted earnings (loss) per share	22,601	18,122

If the anti-dilutive effects of common stock equivalents were considered, shares included in the diluted earnings (loss) per share calculation for the three-month periods ended March 31, 2011 would have included an additional 3.3 million attributable to the exercise of outstanding options and warrants.

(8) Income Taxes

We file numerous consolidated and separate income tax returns with the United States and with many states. With few exceptions, we are no longer subject to U.S. federal, state, or local examinations by tax authorities for years before 2007.

We have subsidiaries in various states that are currently under audit for years ranging from 2003 through 2006. To date, no material adjustments have been proposed as a result of these audits.

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

The Company and its subsidiaries file a consolidated federal income tax return and combined or stand-alone state franchise tax returns for certain states. We utilize the asset and liability method of accounting for income taxes, under which deferred income taxes are recognized for the future tax consequences attributable to the differences between the financial statement values of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date. We have estimated a valuation allowance against that portion of the deferred tax asset whose utilization in future periods is not more than likely. Our net deferred tax asset of $15.0 million as of March 31, 2012 is net of a valuation allowance of $61.4 million.

On a quarterly basis, we determine whether a valuation allowance is necessary for our deferred tax asset. In performing this analysis, we consider all evidence currently available, both positive and negative, in determining whether, based on the weight of that evidence, the deferred tax asset will be realized. We establish a valuation allowance when it is more likely than not that a recorded tax benefit will not be realized. The expense to create the valuation allowance is recorded as additional income tax expense in the period the valuation allowance is established. During the first three months of 2012, we decreased our valuation allowance by $330,000, which was offset by the decrease in our gross deferred tax assets, resulting in no change to the our deferred tax assets and no income tax expense for the period.

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In determining the possible future realization of deferred tax assets, we have considered the taxes paid in the current and prior years that may be available to recapture, as well as future taxable income from the following sources: (a) reversal of taxable temporary differences; and (b) tax planning strategies that, if necessary, would be implemented to accelerate taxable income into years in which net operating losses might otherwise expire. Our tax planning strategies include the prospective sale of certain assets such as finance receivables, residual interests in securitized finance receivables, charged off receivables and base servicing rights. The expected proceeds for such asset sales have been estimated based on our expectation of what buyers of the assets would consider to be reasonable assumptions for net cash flows and required rates of return for each of the various asset types. Our estimates for net cash flows and required rates of return are subjective and inherently subject to future events that may significantly affect actual net proceeds we may receive from executing our tax planning strategies.

We believe such asset sales can produce at least $37.5 million in taxable income within the relevant carryforward period. Such strategies could be implemented without significant effect on our core business or our ability to generate future growth. The costs related to the implementation of these tax strategies were considered in evaluating the amount of taxable income that could be generated in order to realize our deferred tax assets.

(9) Legal Proceedings

Griffith Litigation. We are named as defendant in a putative class action brought in federal district court in Chicago, Illinois. In March 2012 the court gave preliminary approval to a settlement agreed to between us and the plaintiffs, pursuant to which (i) a class will be certified for settlement purposes only, and (ii) we will pay a fixed amount of plaintiff attorney fees and also make payments against claims made by members of the class, the amount of which will be based on class members' responses to our notice of the settlement. Final approval and effectiveness of the settlement will occur only following notice to the class members, a hearing on the fairness of the settlement, and ultimate approval of the settlement following such a hearing. Our legal contingency accrual at March 31, 2012 includes our estimate for the amount that is probable. There can be no assurance as to the ultimate outcome of the case.

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

In November 2001, one of the defendants in the Stanwich Case, Jonathan Pardee, asserted claims for indemnity against us in a separate action, which is now pending in federal district court in Rhode Island. We have filed counterclaims in the Rhode Island federal court against Mr. Pardee, and have filed a separate action against Mr. Pardee's Rhode Island attorneys, in the same court. As of December 31, 2010, these actions in the court in Rhode Island had been stayed, awaiting resolution of an adversary action brought against Mr. Pardee in the bankruptcy court, which is hearing the bankruptcy of Stanwich.

On April 6, 2011, that adversary action was dismissed, pursuant to an agreement between us and the representative of creditors in the Stanwich bankruptcy. Under that agreement, CPS has paid the bankruptcy estate $800,000 and abandoned its claims against the estate, and the estate has abandoned its adversary action against Mr. Pardee. The entire payment in this matter was included in our legal contingency liability as of December 31, 2010. With the dismissal of the adversary action, all known claims asserted against Mr. Pardee have been resolved, without his incurring any liability. Accordingly, we believe that this resolution of the adversary action will result in limitation of our exposure to Mr. Pardee to no more than some portion of his

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attorneys fees incurred. The stay in the action against us in Rhode Island has been lifted, and a trial is scheduled for November 2012.

The reader should consider that any adverse judgment against us in this case for indemnification, in an amount materially in excess of any liability already recorded in respect thereof, could have a material adverse effect on our financial position. There can be no assurance as to the ultimate outcome of this matter.

Other Litigation.

We are routinely involved in various legal proceedings resulting from our consumer finance activities and practices, both continuing and discontinued. We believe that there are substantive legal defenses to such claims, and intend to defend them vigorously. There can be no assurance, however, as to the outcome.

We have recorded a liability as of March 31, 2012 that we believe represents an appropriate allowance for legal contingencies, including those described above. Any adverse judgment against us, if in an amount materially in excess of the recorded liability, could have a material adverse effect on our financial position.

(10) Employee Benefits

On March 8, 2002 we acquired MFN Financial Corporation and its subsidiaries in a merger. We sponsor the MFN Financial Corporation Benefit Plan (the “Plan”). Plan benefits were frozen June 30, 2001. The table below sets forth the Plan’s net periodic benefit cost for the three-month periods ended March 31, 2012 and 2011.

	Three Months Ended March 31,	
	2012	2011
	(In thousands)	
Components of net periodic cost (benefit)		
Service cost	$ -	$ -
Interest Cost	220	228
Expected return on assets	(234)	(237)
Amortization of transition (asset)/obligation	-	-
Amortization of net (gain) / loss	157	112
Net periodic cost (benefit)	$ 143	$ 103

We contributed $137,000 to the Plan during the three-month period ended March 31, 2012 and we anticipate making contributions in the amount of $775,000 for the remainder of 2012.

(11) Fair Value Measurements

In September 2006, the FASB issued ASC 820, "Fair Value Measurements" which clarifies the principle that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. Under the standard, fair value measurements would be separately disclosed by level within the fair value hierarchy.

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

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At the time of issuance, four warrants issued between 2008 and 2010 in conjunction with various debt financing transactions contained features that make them subject to derivative accounting. We valued these warrants using a binomial valuation model using a weighted average volatility assumption of 41%, weighted average term of 8 years and a risk free rate of 3.3%. On March 29, 2012 we amended three of the four warrants to remove the features that resulted in derivative accounting. On the date of the amendment, we valued each of the three warrants using a binomial pricing model as described above. The aggregate value of the three amended warrants of $1.1 million was then reclassified from Accounts payable to Common stock. The remaining warrant subject to derivative accounting was not amended and was valued at March 31, 2012 to be $114,000 and is classified as a liability on our consolidated balance sheet as of March 31, 2012.

In September 2008 we sold automobile contracts in a securitization that was structured as a sale for financial accounting purposes. In that sale, we retained both securities and a residual interest in the transaction that are measured at fair value. We describe below the valuation methodologies we use for the securities retained and the residual interest in the cash flows of the transaction, as well as the general classification of such instruments pursuant to the valuation hierarchy. The securities retained were sold in September 2010 in the re-securitization transaction described in Note 1. In the same transaction, the residual interest was reduced by $1.5 million. The residual interest in such securitization is $4.6 million as of March 31, 2012 and is classified as level 3 in the three-level valuation hierarchy. We determine the value of that residual interest using a discounted cash flow model that includes estimates for prepayments and losses. We use a discount rate of 20% per annum and a cumulative net loss rate of 13%. The assumptions we use are based on historical performance of automobile contracts we have originated and serviced in the past, adjusted for current market conditions. No gain or loss was recorded as a result of the re-securitization transaction described above.

Repossessed vehicle inventory, which is included in Other assets on our balance sheet, is measured at fair value using level 2 assumptions based on our actual loss experience on sale of repossessed vehicles. At March 31, 2012, the finance receivables related to the repossessed vehicles in inventory totaled $8.7 million. We have applied a valuation adjustment of $4.2 million, resulting in an estimated fair value and carrying amount of $4.5 million.

We have no level 3 assets that are measured at fair value on a non-recurring basis. The table below presents a reconciliation for level 3 assets measured at fair value on a recurring basis using significant unobservable inputs:

	Three Months Ended March 31,	
	2012	2011
	(in thousands)	
Residual Interest in Securitizations:		
Balance at beginning of period	$ 4,414	$ 3,841
Cash received during period	(26)	-
Included in earnings	224	144
Balance at end of period	$ 4,612	$ 3,985
Warrant Derivative Liability:		
Balance at beginning of period	$ 967	$ 1,639

Included in earnings		203		(104)
Transfers out of Level 3		(1,056)		-
Balance at end of period	$	114	$	1,535

In September 2011, we acquired $217.8 million of finance receivables from Fireside Bank for a purchase price of $201.3 million. The receivables were acquired by our wholly-owned special purpose subsidiary, CPS Fender Receivables, LLC, which issued a note for $197.3 million, with a fair value of $196.5 million. Since

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the Fireside receivables were originated by another entity with its own underwriting guidelines and procedures, we have elected to account for the Fireside receivables and the related debt secured by those receivables at their estimated fair values so that changes in fair value will be reflected in our results of operations as they occur. Interest income from the receivables and interest expense on the note are included in interest income and interest expense, respectively. Changes to the fair value of the receivables and debt are also to be included in interest income and interest expense, respectively. Our level 3, unobservable inputs reflect our own assumptions about the factors that market participants use in pricing similar receivables and debt, and are based on the best information available in the circumstances. They include such inputs as estimated net charge-offs and timing of the amortization of the portfolio of finance receivables. The table below presents a reconciliation of the acquired finance receivables and related debt measured at fair value on a recurring basis using significant unobservable inputs:

	Three Months Ended March 31,	
	2012	2011
	(in thousands)	
Finance Receivables Measured at Fair Value:		
Balance at beginning of period	$ 160,253	$ -
Payments on finance receivables at fair value	(36,500)	-
Charge-offs on finance receivables at fair value	(2,503)	-
Discount accretion	4,163	-
Mark to fair value	1,510	-
Balance at end of period	$ 126,923	$ -
Debt Secured by Finance Receivables Measured at Fair Value:		
Balance at beginning of period	$ 166,828	$ -
Principal payments on debt at fair value	(39,191)	-
Premium accretion	2,980	-
Mark to fair value	2,400	-
Balance at end of period	133,017	-
Reduction for principal payments collected and payable	(13,270)	-
Adjusted balance at end of period	$ 119,747	$ -

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

	March 31, 2012		December 31, 2011	
	Contractual Balance	Fair Value	Contractual Balance	Fair Value
	(In thousands)			
Fireside receivables portfolio	$ 133,169	$ 126,923	$ 172,167	$ 160,253
Debt secured by Fireside receivables portfolio	123,619	133,017	162,812	166,828

The following summary presents a description of the methodologies and assumptions used to estimate the fair value of our financial instruments. Much of the information used to determine fair value is highly subjective. When applicable, readily available market information has been utilized. However, for a significant portion of our financial instruments, active markets do not exist. Therefore, significant elements of judgment were required in estimating fair

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value for certain items. The subjective factors include, among other things, the estimated timing and amount of cash flows, risk characteristics, credit quality and interest rates, all of which are subject to change. Since the fair value is estimated as of March 31, 2012 and December 31, 2011, the amounts that will actually be realized or paid at settlement or maturity of the instruments could be significantly different. The estimated fair values of financial assets and liabilities at March 31, 2012 and December 31, 2011, were as follows:

Financial Instrument	As of March 31, 2012 (In thousands)				
		Fair Value Measurements Using:			
	Carrying Value	Level 1	Level 2	Level 3	Total
Assets:					
Cash and cash equivalents	$ 10,614	$ 10,614	$ -	$ -	$ 10,614
Restricted cash and equivalents	131,543	131,543	-	-	131,543
Finance receivables, net	543,748	-	-	542,012	542,012
Finance receivables measured at fair value	126,923	-	-	126,923	126,923
Residual interest in securitizations	4,612	-	-	4,612	4,612
Accrued interest receivable	6,380	-	-	6,380	6,380
Liabilities:					
Warrant derivative liability	$ 114	$ -	$ -	$ 114	$ 114
Warehouse lines of credit	28,929	-	-	28,929	28,929
Accrued interest payable	6,135	-	-	6,135	6,135
Residual interest financing	18,015	-	-	18,015	18,015
Securitization trust debt	599,678	-	-	617,762	617,762
Debt secured by receivables measured at fair value	133,017	-	-	133,017	133,017
Senior secured debt	53,570	-	-	53,570	53,570
Subordinated renewable notes	20,741	-	-	20,741	20,741

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	As of December 31, 2011				
Financial Instrument	(In thousands)				
	Fair Value Measurements Using:				
	Carrying Value	Level 1	Level 2	Level 3	Total
Assets:					
Cash and cash equivalents	$ 10,094	10,094	$ -	$ -	$ 10,094
Restricted cash and equivalents	159,228	159,228	-	-	159,228
Finance receivables, net	506,279	-	-	506,647	506,647
Finance receivables measured at fair value	160,253	-	-	160,253	160,253
Residual interest in securitizations	4,414	-	-	4,414	4,414
Accrued interest receivable	6,432	-	-	6,432	6,432
Liabilities:					
Warrant derivative liability	$ 967	-	$ -	$ 967	$ 967
Warehouse lines of credit	25,393	-	-	25,393	25,393
Accrued interest payable	1,239	-	-	1,239	1,239
Residual interest financing	21,884	-	-	21,884	21,884
Securitization trust debt	583,065	-	-	594,224	594,224
Debt secured by receivables measured at fair value	166,828	-	-	166,828	166,828
Senior secured debt	58,344	-	-	58,344	58,344
Subordinated renewable notes	20,750	-	-	20,750	20,750

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The following table provides certain qualitative information about our level 3 fair value measurements:

Financial Instrument	Fair Values as of				Inputs as of	
	March 31,	December 31,			March 31,	December 31,
	2012	2011	Valuation Techniques	Unobservable Inputs	2012	2011
	(In thousands)					
Assets:						
Finance receivables measured at fair value	126,923	160,253	Discounted cash flows	Discount rate	20.4%	20.4%
				Cumulative net losses	5.5%	5.5%
				Monthly average prepayments	0.5%	0.5%
Residual interest in securitizations	4,612	4,414	Discounted cash flows	Discount rate	20.0%	20.0%
				Cumulative net losses	18.3%	18.3%
				Monthly average prepayments	0.5%	0.5%
Liabilities:						
Warrant derivative liability	$ 114	$ 967	Binomial	Stock price	$1.25 / sh	$.89 / sh
				Volatility	36.2%	38.9%
				Risk free rate	1.9%	1.3% -- 1.7%
Debt secured by receivables measured at fair value	133,017	166,828	Discounted cash flows	Discount rate	16.2%	16.2%

Cash, Cash Equivalents and Restricted Cash

The carrying value equals fair value.

Finance Receivables, net

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

Fair Value Receivables and Receivable Financing Debt at Fair Value

The carrying value equals fair value.

Accrued Interest Receivable and Payable

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

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

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

Securitization Trust Debt

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

(12) Liquidity, Results of Operations and Management's Plans

Our business requires substantial cash to support our purchases of automobile contracts and other operating activities. Our primary sources of cash have been cash flows from operating activities, including proceeds from term securitization transactions and other sales of automobile contracts, amounts borrowed under various revolving credit facilities (also sometimes known as warehouse credit facilities), servicing fees on portfolios of automobile contracts previously sold in securitization transactions or serviced for third parties, customer payments of principal and interest on finance receivables, fees for origination of automobile contracts, and releases of cash from securitized pools of automobile contracts in which we have retained a residual ownership interest and from the spread account associated with such pools. Our primary uses of cash have been the purchases of automobile contracts, repayment of amounts borrowed under lines of credit and otherwise, operating expenses such as employee, interest, occupancy expenses and other general and administrative expenses, the establishment of spread account and initial overcollateralization, if any, and the increase of credit enhancement to required levels in securitization transactions, and income taxes. There can be no assurance that internally generated cash will be sufficient to meet our cash demands. The sufficiency of internally generated cash will depend on the performance of securitized pools (which determines the level of releases from those pools and their related spread accounts), the rate of expansion or contraction in our managed portfolio, and the terms upon which we are able to acquire, sell, and borrow against automobile contracts.

We purchase automobile contracts from dealers for a cash price approximating their principal amount, adjusted for an acquisition fee which may either increase or decrease the automobile contract purchase price. Those automobile contracts generate cash flow, however, over a period of years. As a result, we have been dependent on warehouse credit facilities to purchase automobile contracts, and on the availability of cash from outside sources in order to finance our continuing operations, as well as to fund the portion of automobile contract purchase prices not financed under revolving warehouse credit facilities.

The acquisition of automobile contracts for subsequent sale in securitization transactions, and the need to fund spread accounts and initial overcollateralization, if any, and increase credit enhancement levels when those transactions take place, results in a continuing need for capital. The amount of capital required is most heavily dependent on the rate of our automobile contract purchases, the required level of initial credit enhancement in securitizations, and the extent to which the previously established trusts and their related spread accounts either release cash to us or capture cash from collections on securitized automobile contracts. Of those, the factor most subject to our control is the rate at which we purchase automobile contracts.

We are and may in the future be limited in our ability to purchase automobile contracts due to limits on our capital. As of March 31, 2012, we had unrestricted cash of $10.6 million. We had $99.1 million available under the Goldman facility and $7.0 million available under the UBS facility (in all facilities advances are subject to our having purchased available eligible collateral). Our plans to manage our liquidity include maintaining our rate of automobile contract purchases at a level that matches our available capital, and, wherever appropriate, reducing our operating costs. If we are unable to complete such securitizations, we may be unable to increase our rate of automobile contract purchases, in which case our interest income and other portfolio related income would decrease.

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Our liquidity will also be affected by releases of cash from the trusts established with our securitizations. While the specific terms and mechanics of each spread account vary among transactions, our securitization agreements generally provide that we will receive excess cash flows, if any, only if the amount of credit enhancement has reached specified levels and/or the delinquency, defaults or net losses related to the automobile contracts in the pool are below certain predetermined levels. In the event delinquencies, defaults or net losses on the automobile contracts exceed such levels, the terms of the securitization: (i) may require increased credit enhancement to be accumulated for the particular pool; (ii) may restrict the distribution to us of excess cash flows associated with other pools; or (iii) in certain circumstances, may permit the insurers to require the transfer of servicing on some or all of the automobile contracts to another servicer. There can be no assurance that collections from the related trusts will continue to generate sufficient cash. Moreover, most of our spread account balances are pledged as collateral to our residual interest financing. As such, most of the current releases of cash from our securitization trusts are directed to pay the obligations of our residual interest financing.

Our plan for future operations and meeting the obligations of our financing arrangements includes returning to profitability (which we achieved in the fourth quarter of 2011 and the first quarter of 2012) and eliminating our shareholders' deficit by gradually increasing the amount of our contract purchases with the goal of increasing the balance of our outstanding managed portfolio. Our plans also include financing future contract purchases with credit facilities and term securitizations that offer a lower overall cost of funds compared to the facilities we used in 2009 and 2010. To illustrate, in the last six months of 2009 we purchased $6.1 million in contracts and our sole credit facility had a minimum interest rate of 14.00% per annum. By comparison, in 2010, we purchased $113.0 million in contracts and, in March 2010, entered into the $50 million term funding facility which had an interest rate of 11.00% per annum and the ability to decrease such rate to 9.00% per annum if certain conditions were met. In December 2010 we entered into a $100 million credit facility with an interest rate of one-month LIBOR plus 5.00% per annum, with a minimum rate of 6.5% per annum, and in February 2011 we added another $100 million credit facility with an interest rate of one-month LIBOR plus 6.00% per annum. During 2011, we used the two $100 million credit facilities to purchase $284.2 million in new contracts. During the three months ended March 31, 2012 we purchased an additional $119.9 million in new contracts.

Moreover, the weighted average effective coupons of our April 2011, September 2011, December 2011 and March 2012 term securitizations were 3.77%, 4.51%, 4.93% and 3.47%, respectively and did not include financial guaranty policies. These transactions demonstrate our ability to access the lower cost of funds available in the current market environment without the financial guaranties we historically incorporated into our term securitization structures. We expect to complete more term securitizations in 2012. In addition, less competition in the auto financing marketplace has resulted in better terms for our recent contract purchases compared to years before 2008. The following table summarizes the average acquisition fees we charged dealers and the weighted average annual percentage rate on our purchased contracts for the periods shown:

	3 Months Ended March 31, 2012	2011	2010	2009	2008
Average acquisition fee amount	$ 1,079	$ 1,155	$ 1,382	$ 1,508	$ 592
Average acquisition fee as % of amount financed	7.1%	7.4%	9.2%	11.7%	3.9%
Weighted average annual percentage interest rate	20.3%	20.1%	20.1%	19.9%	18.5%

We have and will continue to have a substantial amount of indebtedness. At March 31, 2012, we had approximately $853.9 million of debt outstanding. Such debt consisted primarily of $599.7 million of securitization trust debt, $133.0 in portfolio acquisition debt, $28.9 million of warehouse line of credit debt, $18.0 million of residual interest financing, $53.6 million of senior secured related party debt and $20.7

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million in subordinated notes. We are also currently offering the subordinated notes to the public on a continuous basis, and such notes have maturities that range from three months to 10 years.

As of March 31, 2012 we have a shareholders' deficit of $12.6 million and our recent operating results include net losses of $14.5 million and $33.8 million in 2011 and 2010, respectively. We believe that our results have been materially and adversely affected by the disruption in the capital markets that began in the fourth quarter of 2007, by the recession that began in December 2007, and by related high levels of unemployment. Our ability to repay or refinance maturing debt may be adversely affected by prospective lenders' consideration of our recent operating losses.

Although we believe we are able to service and repay our debt, there is no assurance that we will be able to do so. If our plans for future operations do not generate sufficient cash flows and operating profits, our ability to make required payments on our debt would be impaired. Failure to pay our indebtedness when due could have a material adverse effect and may require us to issue additional debt or equity securities.

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

Overview

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

We were incorporated and began our operations in March 1991. From inception through March 31, 2012, we have purchased a total of approximately $9.2 billion of automobile contracts from dealers. In addition, we obtained a total of approximately $842.0 million of automobile contracts in mergers and acquisitions in 2002, 2003, 2004 and 2011. In 2004 and 2009, we were appointed as a third-party servicer for certain portfolios of automobile receivables originated and owned by non-affiliated entities . Beginning in 2008, our managed portfolio has decreased each year due to our strategy of limiting contract purchases to conserve our liquidity in response to adverse economic conditions, as discussed further below. However, since October 2009, we have gradually increased contract purchases resulting in aggregate purchases of $284.2 million in 2011, compared to $113.0 million in 2010 and $8.6 million in 2009. Our total managed portfolio was $781.8 million at March 31, 2012, compared to $679.7 million at March 31, 2011. The increase between March 31, 2011 and 2012 reflects both our purchases of contracts from dealers and our purchase in September 2011 of a portfolio of $217.8 million of automobile contracts from Fireside Bank, a subsidiary of Kemper Corporation.

We are headquartered in Irvine, California, where most operational and administrative functions are centralized. All credit and underwriting functions are performed in our California headquarters, and we service our automobile contracts from our California headquarters and three servicing branches in Virginia, Florida and Illinois.

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

Securitization and Warehouse Credit Facilities

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

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

Since the third quarter of 2003, we have conducted 28 term securitizations. Of these 28, 22 were periodic (generally quarterly) securitizations of automobile contracts that we purchased from automobile dealers under our regular programs. In addition, in March 2004 and November 2005, we completed securitizations of our retained interests in other securitizations that we and our affiliates previously sponsored. The debt from the March 2004 transaction was repaid in August 2005, and the debt from the November 2005 transaction was repaid in May 2007. Also, in June 2004, we completed a securitization of automobile contracts purchased under our TFC program and acquired in a bulk purchase. Further, in December 2005 and May 2007 we completed securitizations that included automobile contracts purchased under the TFC programs, automobile contracts purchased under the CPS programs and automobile contracts we repurchased upon termination of prior securitizations. Since July 2003 all such securitizations have been structured as secured financings, except that our September 2008 and September 2010 securitizations were in substance sales of the underlying receivables, and were treated as sales for financial accounting purposes.

Our March 2012 securitization included a pre-funding feature in which a portion of the receivables to be pledged to the securitization trust were not scheduled to be delivered to the trust until after the initial closing. As a result, our restricted cash balance at March 31, 2012 included $46.3 million from the proceeds of the sale of the securitization notes that were held by the trustee pending delivery of the remaining receivables. In April 2012, the requisite additional receivables were delivered to the trust and we received the related restricted cash, a significant portion of which was used to repay amounts owed under our warehouse credit facilities.

Portfolio Acquisitions

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

Uncertainty of Capital Markets and General Economic Conditions

We depend upon the availability of warehouse credit facilities and access to long-term financing through the issuance of asset-backed securities collateralized by our automobile contracts. Since 1994, we have completed 54 term securitizations of approximately $7.2 billion in contracts. We conducted four term securitizations in 2006, four in 2007, two in 2008, one in 2010, three in 2011and one in 2012. From July 2003 through April 2008 all of our securitizations were structured as secured financings. The second of our two securitization transactions in 2008 (completed in September 2008) and our securitization in September 2010 (a re-securitization of the remaining receivables from the September 2008 transaction) were each in substance a sale of the related contracts, and have been treated as sales for financial accounting purposes. During 2011, we completed three securitizations of approximately $335.6 million in newly originated contracts, representing our first securitizations of newly originated contracts since April 2008. In March 2012, we completed a $155.0 million securitization that included $117.8 million in newly originated contracts and $37.2 million in seasoned contracts that were previously securitized, but were available as a result of the February 2012 repayment of the bonds associated with those earlier securitizations. All of the 2011 and 2012 securitizations were structured as secured financings.

From the fourth quarter of 2007 through the end of 2009, we observed unprecedented adverse changes in the market for securitized pools of automobile contracts. These changes included reduced liquidity, and reduced demand for asset-backed securities, particularly for securities carrying a financial guaranty and for securities backed by sub-prime automobile receivables. Moreover, many of the firms that previously provided financial guarantees, which were an integral part of our securitizations, suspended offering such guarantees. The adverse changes that took place in the market from the fourth quarter of 2007 through the end of 2009 caused us to conserve liquidity by significantly reducing our purchases of automobile contracts. However, since October 2009, we have gradually increased our contract purchases by utilizing one $50 million revolving credit facility that we established in September 2009 and another $50 million term funding facility that we established in March 2010. In September 2010 we took advantage of improvement in the market for asset-backed securities by re-securitizing the remaining underlying receivables from our unrated September 2008 securitization. By doing so we were able to pay off the bonds associated with the September 2008 transaction and issue rated bonds with a significantly lower weighted average coupon. The September 2010 transaction was our first rated term securitization since 1993 that did not utilize a financial guaranty. More recently, we increased our short-term funding capacity by $200 million with the establishment of a new $100 million credit facility in December 2010 and an additional $100 million credit facility in February 2011. The September 2009 revolving facility terminated in September 2011, and the March 2010 term facility was fully utilized by December 2010. In February 2012, we amended the February 2011 facility to extend the revolving period from February 2012 to May 2012 and reduced the maximum advance from $100 million to $35 million. Our current maximum revolving warehouse financing capacity is $135 million. Since the beginning of 2011, we have completed four securitizations of approximately $490.6 million in receivables. In spite of the improvements we have seen in the capital markets, if the trend of improvement in the markets for asset-backed securities should reverse, or if we should be unable to obtain additional credit facilities or to complete additional term securitizations, we may curtail or cease our purchases of new automobile contracts, which could lead to a material adverse effect on our operations.

The downturn in economic conditions and the capital markets that began in the fourth quarter of 2007 has negatively affected many aspects of our industry. First, throughout 2008 and 2009 there was reduced demand for asset-backed securities secured by consumer finance receivables, including sub-prime automobile receivables, as compared to 2007 and earlier. During 2010, however, we observed that yield requirements for investors that purchase securities backed by consumer finance receivables, including sub-prime automobile receivables, decreased significantly and approached pre-2008 levels, albeit with significantly fewer transactions in the market. Second, there have been fewer lenders who provide short-term warehouse credit facilities for sub-prime automobile finance companies due to more uncertainty regarding the prospects of obtaining long-term financing through the issuance of asset-backed securities than before 2008. Many capital market participants such as investment banks, financial guaranty providers and institutional investors who previously played a role in the sub-prime auto finance industry have withdrawn from the industry, or in some cases, have ceased to do business. These developments resulted in our incurring higher interest costs for receivables we financed in 2009 and 2010 compared to pre-2008 levels. However, in December 2010 we entered into a $100 million two-year warehouse credit line with a significantly lower cost of funds than the facilities we used in 2009 and 2010. Finally, broad economic weakness and high levels of unemployment from 2008 onward have made many of our customers less willing or able to pay, resulting in higher delinquencies, charge-offs and losses. Each of these factors has adversely affected our results of operations. Should existing economic conditions worsen, both our ability to purchase new contracts and the performance of our existing managed portfolio may be impaired, which, in turn, could have a further material adverse effect on our results of operations.

Financial Covenants

Certain of our securitization transactions, our warehouse credit facilities and our residual interest financing contain various financial covenants requiring certain minimum financial ratios and results. Such covenants include maintaining minimum levels of liquidity and net worth and not exceeding maximum leverage levels. As of March 31, we were in compliance with all such covenants. In addition, certain securitization and non-securitization related debt contain cross-default provisions that would allow certain creditors to declare a default if a default occurred under a different facility.

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Results of Operations

Comparison of Operating Results for the three months ended March 31, 2012 with the three months ended March 31, 2011

Revenues. During the three months ended March 31, 2012, revenues were $44.5 million, an increase of $12.1 million, or 37.4%, from the prior year revenue of $32.4 million. The primary reason for the increase in revenues is an increase in interest income. Interest income for the three months ended March 31, 2012 increased $12.0 million, or 42.1%, to $40.6 million from $28.6 million in the prior year. The primary reason for the increase in interest income is the increase in finance receivables held by consolidated subsidiaries which increased from $546.3 at March 31, 2011 to $721.6 at March 31, 2012.

Servicing fees totaling $801,000 in the three months ended March 31, 2012 decreased $615,000, or 43.4%, from $1.4 million in the prior year. The decrease in servicing fees is due to the amortization and resulting decrease in the principal balance of the two portfolios on which we earn base servicing fees. We earned base servicing fees on our September 2010 term securitization transaction (a re-securitization of the remaining receivables from the September 2008 securitization, treated as a sale for financial accounting purposes) and on a portfolio of sub-prime automobile receivables owned by a bankruptcy remote subsidiary of CompuCredit Corporation. As of March 31, 2012 and 2011, our managed portfolio owned by consolidated vs. non-consolidated subsidiaries and other third parties was as follows:

	March 31, 2012				March 31, 2011			
		Amount	% (1)			Amount	% (1)	
Total Managed Portfolio			($ in millions)					
Owned by Consolidated Subsidiaries								
CPS Originated Receivables	$	588.4	75.3	%	$	546.3	80.4	%
Fireside		133.2	17.0	%		-	0.0	%
Owned by Non-Consolidated Subsidiaries		34.4	4.4	%		71.6	10.5	%
Third-Party Servicing Portfolios		25.8	3.3	%		61.8	9.1	%
Total	$	781.8	100.0	%	$	679.7	100.0	%

At March 31, 2012, we were generating income and fees on a managed portfolio with an outstanding principal balance of $781.8 million (this amount includes $34.4 million of automobile contracts on which we earn servicing fees and a residual interest and also includes another $25.8 million of automobile contracts on which we earn servicing fees and own a note collateralized by such contracts), compared to a managed portfolio with an outstanding principal balance of $679.7 million as of March 31, 2011. At March 31, 2012 and 2011, the managed portfolio composition was as follows:

	March 31, 2012				March 31, 2011			
		Amount	%			Amount	%	
Originating Entity			($ in millions)					
CPS	$	621.7	79.5	%	$	611.6	90.0	%
Fireside		133.2	17.0	%		-	0.0	%
TFC		1.1	0.1	%		6.3	0.9	%
Third Party Portfolio		25.8	3.3	%		61.8	9.1	%

Total	$	781.8	100.0	%	$	679.7	100.0	%

Other income increased by $710,000, or 29.6%, to $3.1 million in the three months ended March 31, 2012 from $2.4 million during the prior year. The year-over-year increase is the result of an increase of $422,000 in income from direct

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mail and related products and services that we offer to our dealers, the recognition of $355,000 in other income related to a mark up of the fair value of the receivables associated with the Fireside acquisition and an increase of $118,000 in remittances from third-party providers of convenience fees paid by our customers for web based and other electronic payments. The increases in other income were offset by a decrease of $76,000 in sales tax refunds and a decrease of $104,000 in recoveries on receivables from the 2002 acquisition.

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

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

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

Total operating expenses were $44.0 million for the three months ended March 31, 2012, compared to $36.6 million for the prior year, an increase of $7