

CONSUMER PORTFOLIO SERVICES INC  
Form 10-Q  
November 06, 2007

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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 SEPTEMBER 30, 2007

COMMISSION FILE NUMBER: 0-51027

CONSUMER PORTFOLIO SERVICES, INC.  
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

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

16355 Laguna Canyon Road, Irvine, California 92618  
(Address of principal executive offices) (Zip Code)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (949) 753-6800

FORMER NAME, FORMER ADDRESS AND FORMER FISCAL YEAR, IF CHANGED SINCE LAST  
REPORT: N/A

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

Indicate by check mark whether the registrant is a large accelerated filer or a  
non-accelerated filer. See definition of "accelerated filer and large  
accelerated filer" in Rule 12b-2 of the Exchange Act.  
Large Accelerated Filer [ ] Accelerated Filer [X] Non-Accelerated Filer [ ]

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 October 26, 2007 the registrant had 19,838,732 common shares outstanding.

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CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES  
INDEX TO FORM 10-Q  
FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2007

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### ITEM 1. FINANCIAL STATEMENTS

#### CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS (IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

|   | SEPTEMBER 30,<br>2007 | DECEMBER 31,<br>2006 |
|---|-----------------------|----------------------|
|   | -----                 | -----                |
| ASSETS                                    |                       |                      |
| Cash and cash equivalents                 | \$ 16,907             | \$ 14,215            |
| Restricted cash and equivalents           | 258,060               | 193,001              |
| Finance receivables                       | 1,997,106             | 1,480,794            |
| Less: Allowance for finance credit losses | (99,675)              | (79,380)             |

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|  |              |              |
|--|--------------|--------------|
| Finance receivables, net   | 1,897,431    | 1,401,414    |
| Residual interest in securitizations   | 1,551        | 13,795       |
| Furniture and equipment, net   | 1,211        | 824          |
| Deferred financing costs, net  | 17,910       | 12,702       |
| Deferred tax assets, net   | 55,911       | 54,669       |
| Accrued interest receivable  | 22,406       | 17,043       |
| Other assets   | 22,198       | 20,931       |
|  | -----        | -----        |
|  | \$ 2,293,585 | \$ 1,728,594 |
|  | =====        | =====        |
|  |              |              |
| LIABILITIES AND SHAREHOLDERS' EQUITY   |              |              |
| LIABILITIES  |              |              |
| Accounts payable and accrued expenses  | \$ 23,027    | \$ 20,888    |
| Warehouse lines of credit  | 79,185       | 72,950       |
| Income taxes payable   | 12,782       | 10,297       |
| Residual interest financing  | 60,000       | 31,378       |
| Securitization trust debt  | 1,984,023    | 1,442,995    |
| Senior secured debt, related party   | -            | 25,000       |
| Subordinated renewable notes   | 22,065       | 13,574       |
|  | -----        | -----        |
|  | 2,181,082    | 1,617,082    |
|  |              |              |
| COMMITMENTS AND CONTINGENCIES  |              |              |
| SHAREHOLDERS' EQUITY   |              |              |
| Preferred stock, \$1 par value;<br>authorized 5,000,000 shares; none issued  | -            | -            |
| Series A preferred stock, \$1 par value;<br>authorized 5,000,000 shares;<br>3,415,000 shares issued; none outstanding  | -            | -            |
| Common stock, no par value; authorized<br>30,000,000 shares; 19,831,082 and 21,504,688<br>shares issued and outstanding at September 30, 2007 and<br>December 31, 2006, respectively | 56,129       | 64,438       |
| Additional paid in capital, warrants   | 794          | 794          |
| Retained earnings  | 57,331       | 48,031       |
| Accumulated other comprehensive loss   | (1,751)      | (1,751)      |
|  | -----        | -----        |
|  | 112,503      | 111,512      |
|  | -----        | -----        |
|  | \$ 2,293,585 | \$ 1,728,594 |
|  | =====        | =====        |

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  
SEPTEMBER 30,

NINE MONTHS ENDED  
SEPTEMBER 30,

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|   | 2007      | 2006      | 2007      | 2006      |
|---|-----------|-----------|-----------|-----------|
|   | -----     | -----     | -----     | -----     |
| <b>Revenues:</b>  |           |           |           |           |
| Interest income   | \$ 97,423 | \$ 70,623 | \$267,361 | \$188,189 |
| Servicing fees  | 274       | 633       | 668       | 2,436     |
| Other income  | 5,058     | 2,457     | 17,020    | 8,344     |
|   | -----     | -----     | -----     | -----     |
|   | 102,755   | 73,713    | 285,049   | 198,969   |
|   | -----     | -----     | -----     | -----     |
| <b>EXPENSES:</b>  |           |           |           |           |
| Employee costs  | 11,566    | 9,273     | 33,704    | 28,349    |
| General and administrative                                    | 6,335     | 6,159     | 18,386    | 16,948    |
| Interest  | 36,317    | 23,649    | 97,954    | 61,469    |
| Interest, related party                                       | 65        | 1,426     | 1,646     | 3,943     |
| Provision for credit losses                                   | 36,300    | 24,045    | 98,458    | 65,322    |
| Marketing   | 4,755     | 3,617     | 13,681    | 10,740    |
| Occupancy   | 949       | 1,075     | 2,815     | 2,920     |
| Depreciation and amortization                                 | 128       | 204       | 418       | 596       |
|   | -----     | -----     | -----     | -----     |
|   | 96,415    | 69,448    | 267,062   | 190,287   |
|   | -----     | -----     | -----     | -----     |
| Income before income tax expense                              | 6,340     | 4,265     | 17,987    | 8,682     |
| Income tax expense  | 2,663     | -         | 7,591     | -         |
|   | -----     | -----     | -----     | -----     |
| Net income  | \$ 3,677  | \$ 4,265  | \$ 10,396 | \$ 8,682  |
|   | =====     | =====     | =====     | =====     |
| <b>Earnings per share:</b>                                    |           |           |           |           |
| Basic   | \$ 0.18   | \$ 0.20   | \$ 0.49   | \$ 0.40   |
| Diluted   | 0.16      | 0.18      | 0.45      | 0.36      |
| <b>Number of shares used in computing earnings per share:</b> |           |           |           |           |
| Basic   | 20,779    | 21,840    | 21,279    | 21,804    |
| Diluted   | 22,438    | 23,850    | 23,184    | 24,139    |

SEE ACCOMPANYING NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

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

|   | NINE MONTHS ENDED<br>SEPTEMBER 30, |          |
|---|------------------------------------|----------|
|   | -----                              | -----    |
|   | 2007                               | 2006     |
|   | -----                              | -----    |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>                                      |                                    |          |
| Net income  | \$ 10,396                          | \$ 8,682 |
| Adjustments to reconcile net income to net cash provided by operating activities: |                                    |          |
| Write up on residual asset  | (4,820)                            | -        |
| Amortization of deferred acquisition fees   | (10,662)                           | (8,632)  |
| Amortization of discount on Class B Notes   | 3,337                              | 1,897    |

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|  |             |           |
|--|-------------|-----------|
| Depreciation and amortization                                | 418         | 596       |
| Amortization of deferred financing costs                     | 6,670       | 4,385     |
| Provision for credit losses                                  | 98,459      | 65,322    |
| Stock-based compensation expense                             | 786         | -         |
| Interest income on residual assets                           | (2,210)     | (3,893)   |
| Cash received from residual interest in securitizations      | 19,274      | 11,266    |
| Changes in assets and liabilities:                           |             |           |
| Restricted cash and equivalents                              | (65,058)    | (39,412)  |
| Accrued interest receivable                                  | (5,363)     | (3,446)   |
| Other assets   | (1,380)     | (5,499)   |
| Tax assets   | (1,242)     | (10,858)  |
| Accounts payable and accrued expenses                        | 2,138       | 2,448     |
| Tax liabilities  | 1,390       | -         |
|  | -----       | -----     |
| Net cash provided by (used in) operating activities          | 52,133      | 22,856    |
| <br>CASH FLOWS FROM INVESTING ACTIVITIES:                    |             |           |
| Purchases of finance receivables held for investment         | (1,016,547) | (777,622) |
| Proceeds received on finance receivables held for investment | 432,732     | 329,214   |
| Purchase of furniture and equipment                          | (692)       | (261)     |
|  | -----       | -----     |
| Net cash used in investing activities                        | (584,507)   | (448,669) |
| <br>CASH FLOWS FROM FINANCING ACTIVITIES:                    |             |           |
| Proceeds from issuance of securitization trust debt          | 1,035,864   | 786,052   |
| Proceeds from issuance of subordinated renewable notes       | 10,927      | 5,725     |
| Payments on subordinated renewable notes                     | (2,436)     | (566)     |
| Net proceeds from warehouse lines of credit                  | 6,235       | 29,466    |
| Proceeds (repayment) of residual interest financing debt     | 28,622      | (19,503)  |
| Repayment of securitization trust debt                       | (498,174)   | (356,252) |
| Repayment of senior secured debt                             | (25,000)    | -         |
| Repayment of subordinated debt                               | -           | (14,000)  |
| Payment of financing costs                                   | (11,877)    | (7,024)   |
| Repurchase of common stock                                   | (10,407)    | (2,508)   |
| Tax benefit from exercise of stock options                   | 238         | 634       |
| Exercise of options and warrants                             | 1,074       | 1,302     |
|  | -----       | -----     |
| Net cash provided by financing activities                    | 535,066     | 423,326   |
|  | -----       | -----     |
| Decrease in cash   | 2,692       | (2,487)   |
| Cash at beginning of period                                  | 14,215      | 17,789    |
|  | -----       | -----     |
| Cash at end of period  | \$ 16,907   | \$ 15,302 |
|  | =====       | =====     |
| <br>Supplemental disclosure of cash flow information:        |             |           |
| Cash paid during the period for:                             |             |           |
| Interest   | \$ 87,462   | \$ 57,943 |
| Income taxes   | \$ 7,205    | \$ 10,110 |

SEE ACCOMPANYING NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

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### (1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### DESCRIPTION OF BUSINESS

We were formed in California on March 8, 1991. We specialize primarily 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. We do not currently lend money directly to consumers, although we intend to do so in the future. To date, we have purchased installment automobile contracts from Dealers based on the guidelines of our financing programs (the "CPS programs").

#### 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 10 of Regulation S-X of the Securities and Exchange Commission, and include all adjustments that are, in our opinion, necessary for a fair presentation of the results for the interim period presented. All such adjustments are, in our opinion, 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 and nine-month periods ended September 30, 2007 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, 2006.

#### OTHER INCOME

Other Income consists primarily of gains recognized on our Residual interest in securitizations, recoveries on previously charged off CPS and MFN contracts, fees paid to us by Dealers for certain direct mail services we provide and, in 2007, \$1.7 million in proceeds from the sale of previously charged-off receivables to an independent third party. The gain recognized related to the residual interest was \$4.8 million for the nine months ended September 30, 2007. There were no gains recognized for the same period in 2006. The recoveries on the charged-off CPS and MFN contracts were \$2.4 million and \$3.4 million for the nine months ended September 30, 2007 and 2006, respectively. The direct mail revenues were \$3.9 million and \$2.9 million for the same period in 2007 and 2006, respectively.

#### STOCK-BASED COMPENSATION

Effective January 1, 2006, we adopted Statement of Financial Accounting Standards No. 123(R), "Share-Based Payment, revised 2004" ("SFAS 123R"), prospectively for all option awards granted, modified or settled after January 1, 2006, using the modified prospective method. Under this method, we recognize compensation costs in the financial statements for all share-based payments granted subsequent to January 1, 2006 based on the grant date fair value

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estimated in accordance with the provisions of SFAS 123(R).

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

For the nine months ended September 30, 2007, we recorded stock-based compensation costs in the amount of \$786,000. As of September 30, 2007, unrecognized stock-based compensation costs to be recognized over future periods equaled \$4.4 million. This amount will be recognized as expense over a weighted-average period of 4.2 years. For the nine months ended September 30, 2006, we recorded no stock-based compensation costs as there were no option awards granted during the nine-month period ended September 30, 2006 and there was no vesting of option awards for options granted prior to January 1, 2006 since all options outstanding as of December 31, 2005 were fully vested at that time.

The following represents stock option activity for the nine months ended September 30, 2007:

|   | NUMBER OF<br>SHARES<br>(IN THOUSANDS) | WEIGHTED<br>AVERAGE<br>EXERCISE PRICE | W<br>A<br>RE<br>CONTR |
|---|---------------------------------------|---------------------------------------|-----------------------|
|   | -----                                 | -----                                 | -----                 |
| Options outstanding at the beginning of period..... | 5,352                                 | \$ 4.11                               |                       |
| Granted.....  | 1,142                                 | 5.90                                  |                       |
| Exercised.....                                      | (328)                                 | 3.25                                  |                       |
| Forefeited.....                                     | (55)                                  | 6.78                                  |                       |
|   | -----                                 | -----                                 | -----                 |
| Options outstanding at the end of period.....       | 6,111                                 | \$ 4.47                               | 7.                    |
|   | =====                                 | =====                                 | =====                 |
| Options exercisable at the end of period.....       | 4,165                                 | \$ 3.62                               | 6.                    |
|   | =====                                 | =====                                 | =====                 |

At September 30, 2007, the aggregate intrinsic value of options outstanding and exercisable was \$7.4 million and \$8.6 million, respectively. The total intrinsic value of options exercised was \$973,000 and \$1.8 million for the nine months ended September 30, 2007 and 2006, respectively. New shares were issued for all options exercised during the three-month and nine-month periods ended September 30, 2007 and 2006. At our annual meeting of shareholders held on June 26, 2007, the shareholders approved an amendment to our 2006 Long-Term Equity Incentive Plan that increased the number of shares issuable from 1,500,000 to 3,000,000. There were 1.0 million shares available for future stock option grants under existing plans as of September 30, 2007.

We use the Black-Scholes option valuation model to estimate the fair value of each option on the date of grant, using the assumptions noted in the following table. We did not disclose assumptions for the nine months ended September 30, 2006 because there were no options granted in the period. The expected term of options granted is computed as the mid-point between the vesting date and the end of the contractual term. The risk-free rate is based on U.S. Treasury instruments in effect at the time of grant whose terms are consistent with the expected term of our stock options. Expected volatility is based on historical

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volatility of our stock. The dividend yield is based on historical experience and the lack of any expected future changes.

|                              | NINE MONTHS ENDED<br>SEPTEMBER 30, |
|------------------------------|------------------------------------|
|                              | -----<br>2007<br>-----             |
| Risk-free interest rate..... | 4.56%                              |
| Expected term, in years..... | 5.9                                |
| Expected volatility.....     | 46.35%                             |
| Dividend yield.....          | 0%                                 |

### PURCHASES OF COMPANY STOCK

During the nine-month periods ended September 30, 2007 and 2006, we purchased 2,002,856 and 395,356 shares, respectively, of our common stock, at average prices of \$5.20 and \$6.34, respectively.

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

#### NEW ACCOUNTING PRONOUNCEMENTS

In February 2006, the FASB issued FASB Statement No. 155, "Accounting for Certain Hybrid Instruments". This statement amends the guidance in FASB Statements No. 133, "Accounting for Derivative Instruments and Hedging Activities", and No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities". Statement 155 allows financial instruments that have embedded derivatives to be accounted for as a whole (eliminating the need to bifurcate the derivative from its host) if the holder elects to account for the whole instrument on a fair value basis. The Statement also amends Statement 140 to eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. Statement 155 is effective for all financial instruments acquired or issued after January 1, 2007. The adoption of this statement did not have a material effect on our financial position or operations.

In March 2006, the FASB issued FASB Statement No. 156, "Accounting for the Servicing of Financial Assets an Amendment to FASB Statement No. 140" (FAS 156). With respect to the accounting for separately recognized servicing assets and servicing liabilities, this statement: (1) requires an entity to recognize a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a specific types of servicing contracts identified in the statement, (2) requires that all separately recognized servicing assets and servicing liabilities be initially measured at fair value, if practicable, (3) permits an entity to choose subsequent measurement methods for each class of separately recognized servicing assets and servicing liabilities, (4) permits a one-time reclassification of available-for-sale securities to trading securities by entities with recognized servicing rights at the initial adoption of this statement, and (5) requires a separate presentation of servicing assets and servicing liabilities subsequently measured at fair value in the statement of financial position and additional disclosures for all separately recognized servicing assets and servicing liabilities. FAS 156 became effective for us on January 1, 2007. The adoption of



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this statement did not have a significant effect on our financial position or results of operations.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"). SFAS No. 157 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. SFAS 157 is effective for us on January 1, 2008. We are in the process of evaluating SFAS 157 and do not believe it will have a significant effect on our financial position or results of operations.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities-Including an Amendment of FASB Statement No. 115" ("SFAS 159"). SFAS 159 permits an entity to choose to measure many financial instruments and certain other items at fair value. Most of the provisions of SFAS 159 are elective, however, the amendment to SFAS 115, "Accounting for Certain Investments in Debt and Equity Securities", applies to all entities with available for sale or trading securities. SFAS 159 is elective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. We are currently assessing this Statement to determine whether or not we would elect to measure any financial instruments at their fair value.

In June 2006, the FASB issued Interpretation No. 48 "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement 109" ("FIN 48"). FIN 48 establishes a single model to address accounting for uncertain tax positions. FIN 48 clarifies the accounting for income taxes by prescribing a minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN 48 also provides guidance on derecognition, measurement classification, interest and penalties, accounting in interim periods, disclosure and transition. Upon adoption as of January 1, 2007, we increased our existing reserves for uncertain tax positions by \$1.1 million, largely related to state income tax matters. The increase was recorded as a cumulative effect adjustment to shareholders' equity.

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

#### RECENT DEVELOPMENTS

In July 2007, we opened a combination term and revolving residual credit facility, and used a portion of our initial draw under that facility to repay our remaining outstanding senior secured indebtedness and residual interest financing debt.

Under this facility, we have used and intend to use eligible residual interests in securitizations as collateral for floating rate borrowings. The amount that may be borrowed is computed using an agreed valuation methodology of the residuals, subject to an overall maximum principal amount of \$120 million that may be borrowed, represented by (i) a \$60 million Class A-1 Variable Funding Note (the "Revolving Note"), and (ii) a \$60 million Class A-2 Term Note (the "Term Note"). The facility's revolving feature is to expire by its terms in July 2008. The \$60 million Term Note was drawn in July 2007 and is due in July 2009.

(2) FINANCE RECEIVABLES

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The following table presents the components of Finance Receivables, net of unearned interest and deferred acquisition fees and originations costs:

|  | SEPTEMBER 30,<br>2007 | DECEMBER<br>20 |
|--|-----------------------|----------------|
|  | -----                 | -----          |
|  | (IN THOUSANDS)        |                |
| Finance Receivables  |                       |                |
| Automobile   |                       |                |
| Simple Interest.....                                       | \$ 2,005,486          | \$ 1,4         |
| Pre-compute, net of unearned interest.....                 | 17,750                |                |
|  | -----                 | -----          |
| Finance Receivables, net of unearned interest.....         | 2,023,236             | 1,5            |
| Less: Unearned acquisition fees and originations costs.... | (26,130)              | (              |
|  | -----                 | -----          |
| Finance Receivables.....                                   | \$ 1,997,106          | \$ 1,4         |
|  | =====                 | =====          |

The following table presents a summary of the activity for the allowance for credit losses for the nine-month periods ended September 30, 2007 and 2006:

|   | SEPTEMBER 30,<br>2007 | SEPTEMBER<br>20 |
|---|-----------------------|-----------------|
|   | -----                 | -----           |
|   | (IN THOUSANDS)        |                 |
| Balance at beginning of period.....                     | \$ 79,380             | \$              |
| Provision for credit losses on finance receivables..... | 98,458                |                 |
| Charge offs.....  | (96,220)              | (               |
| Recoveries.....   | 18,057                |                 |
|   | -----                 | -----           |
| Balance at end of period.....                           | \$ 99,675             | \$              |
|   | =====                 | =====           |

(3) RESIDUAL INTEREST IN SECURITIZATIONS

The residual interest in securitizations represents the discounted sum of expected future cash flows from securitization trusts held by non-consolidated subsidiaries and certain cash flows of receivables from terminated trusts. The following table presents the components of the residual interest in securitizations, which are shown at their discounted amounts:

|  | SEPTEMBER 30,<br>2007 | DECEMBER<br>20 |
|--|-----------------------|----------------|
|  | -----                 | -----          |
|  | (IN THOUSANDS)        |                |

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|   |    |       |       |
|---|----|-------|-------|
| Cash, commercial paper, United States government securities and other qualifying investments (Spread Accounts)..... | \$ | -     | \$    |
| Receivables from trusts (NIRs) and other cash flows .....   |    | 1,551 |       |
| Overcollateralization.....  |    | -     |       |
|   |    | ----- | ----- |
| Residual interest in securitizations.....   | \$ | 1,551 | \$    |
|   |    | ----- | ----- |

The following table presents estimated remaining undiscounted credit losses included in the fair value estimate of the residuals as a percentage of our managed portfolio held by non-consolidated subsidiaries subject to recourse provisions:

|  |    |                      |
|--|----|----------------------|
|  |    | DECEMBER 31,<br>2006 |
|  |    | -----                |
| Undiscounted estimated credit losses.....  | \$ | 1,759                |
| Managed portfolio held by non-consolidated subsidiaries.....   |    | 34,850               |
| Undiscounted estimated credit losses as percentage of managed portfolio held by non-consolidated subsidiaries..... |    | 5.05%                |

The key economic assumptions used in measuring all residual interests in securitizations as of December 31, 2006 are included in the table below. As of September 30, 2007 we have exercised our call option on all unconsolidated securitization transactions that were outstanding as December 31, 2006. The remaining residual asset relates to an estimate of cash flows from charged off receivables related to our securitizations from 2001 to 2003, for which we have used a discount rate of 25%, which is consistent with previous periods.

|                                     |                |                      |
|-------------------------------------|----------------|----------------------|
|                                     |                | DECEMBER 31,<br>2006 |
|                                     |                | -----                |
| Prepayment speed (Cumulative).....  | 22.7% - 32.5%  |                      |
| Net credit losses (Cumulative)..... | 11.8% - 15.4%  |                      |
| Expected call date .....            | September 2007 |                      |

(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:

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| Series | Final Scheduled Payment Date (1) | Receivables Pledged at September 30, 2007 | Initial Principal | Outstanding Principal at September 30, 2007 | Outstanding Principal at December 31, 2006 |
|--------|----------------------------------|---|-------------------|---|--|
| -----  | -----                            | -----                                     | -----             | -----                                       | -----                                      |

(DOLLARS IN THOUSANDS)

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|                |               |              |              |              |              |
|----------------|---------------|--------------|--------------|--------------|--------------|
| CPS 2003-C     | March 2010    | \$ 7,577     | \$ 87,500    | \$ 7,493     | \$ 14,815    |
| CPS 2003-D     | October 2010  | 8,636        | 75,000       | 8,350        | 15,191       |
| CPS 2004-A     | October 2010  | 11,948       | 82,094       | 12,239       | 21,608       |
| PCR 2004-1     | N/A           | -            | 76,257       | -            | 8,097        |
| CPS 2004-B     | February 2011 | 17,661       | 96,369       | 17,780       | 29,437       |
| CPS 2004-C     | April 2011    | 22,107       | 100,000      | 22,109       | 35,480       |
| CPS 2004-D     | December 2011 | 30,472       | 120,000      | 30,244       | 47,384       |
| CPS 2005-A     | October 2011  | 42,454       | 137,500      | 39,718       | 62,610       |
| CPS 2005-B     | February 2012 | 49,450       | 130,625      | 45,414       | 70,933       |
| CPS 2005-C     | March 2012    | 83,419       | 183,300      | 77,963       | 117,434      |
| CPS 2005-TFC   | July 2012     | 30,603       | 72,525       | 29,153       | 45,444       |
| CPS 2005-D     | July 2012     | 71,978       | 145,000      | 70,263       | 100,615      |
| CPS 2006-A     | November 2012 | 138,869      | 245,000      | 136,882      | 195,822      |
| CPS 2006-B     | January 2013  | 165,504      | 257,500      | 161,961      | 224,478      |
| CPS 2006-C     | June 2013     | 180,787      | 247,500      | 177,404      | 236,139      |
| CPS 2006-D     | August 2013   | 179,415      | 220,000      | 176,042      | 217,508      |
| CPS 2007-A     | November 2013 | 259,432      | 290,000      | 253,828      | N/A          |
| CPS 2007-TFC   | December 2013 | 97,909       | 113,293      | 95,950       | N/A          |
| CPS 2007-B     | January 2014  | 301,488      | 314,999      | 298,860      | N/A          |
| CPS 2007-C (2) | May 2014      | 228,305      | 294,750      | 322,370      | N/A          |
|                |               | -----        | -----        | -----        | -----        |
|                |               | \$ 1,928,014 | \$ 3,289,212 | \$ 1,984,023 | \$ 1,442,995 |
|                |               | =====        | =====        | =====        | =====        |

- (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 \$182.3 MILLION IN 2007, \$584.5 MILLION IN 2008, \$449.5 MILLION IN 2009, \$337.4 MILLION IN 2010, \$254.5 MILLION IN 2011, \$150.0 MILLION IN 2012 AND \$25.8 MILLION IN 2013.
- (2) RECEIVABLES PLEDGED AT SEPTEMBER 30, 2007 EXCLUDES APPROXIMATELY \$96.6 MILLION IN AUTOMOBILE CONTRACTS DELIVERED TO THIS TRUST IN OCTOBER 2007 PURSUANT TO A PRE-FUNDING STRUCTURE.

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 \$1.8 billion, 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 and the warehouse credit facilities require that certain delinquency and credit loss criteria be met with respect to the collateral pool, and require that we maintain minimum levels of liquidity and net worth and not exceed maximum leverage levels and maximum financial losses. In addition, certain securitization and non-securitization related debt contain cross-default provisions, which would allow certain creditors to declare a default if a default were declared under a different facility. As of September 30, 2007, we were in compliance with all such financial covenants.

We are responsible for the administration and collection of the automobile contracts. The securitization agreements also require certain funds be held in restricted cash accounts to provide additional collateral for the borrowings, to purchase retail installment contracts that the securitization trust has committed to buy, or to be applied to make payments on the securitization trust debt. As of September 30, 2007, restricted cash under the various agreements

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totalled approximately \$258.1 million. That figure includes \$96.6 million held by our CPS 2007-C securitization trust which was used to purchase additional automobile contracts in October 2007. Interest expense on the securitization trust debt is composed 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 subordinated notes. Deferred financing costs and discounts on subordinated notes related to the securitization trust debt are amortized using a level yield method. Accordingly, the effective cost of borrowing of the securitization trust debt is greater than the stated rate of interest.

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 warehouse lines of credit. 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 of ours.

(5) INTEREST INCOME

The following table presents the components of interest income:

|                                      | THREE MONTHS ENDED<br>SEPTEMBER 30, |           | NINE MONTHS ENDED<br>SEPTEMBER 30, |            |
|--------------------------------------|-------------------------------------|-----------|------------------------------------|------------|
|                                      | 2007                                | 2006      | 2007                               | 2006       |
|                                      | (IN THOUSANDS)                      |           | (IN THOUSANDS)                     |            |
| Interest on Finance Receivables..... | \$ 94,665                           | \$ 67,128 | \$ 258,433                         | \$ 179,875 |
| Residual interest income.....        | 524                                 | 1,729     | 2,210                              | 3,893      |
| Other interest income.....           | 2,234                               | 1,766     | 6,718                              | 4,421      |
| Net interest income.....             | \$ 97,423                           | \$ 70,623 | \$ 267,361                         | \$ 188,189 |

(6) EARNINGS PER SHARE

Earnings per share for the nine-month periods ended September 30, 2007 and 2006 were calculated using the weighted average number of shares outstanding for the related period. The following table reconciles the number of shares used in the computations of basic and diluted earnings per share for the nine-month periods ended September 30, 2007 and 2006:

THREE MONTHS ENDED

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|  | SEPTEMBER 30,  |        |
|--|----------------|--------|
|  | 2007           | 2006   |
|  | (IN THOUSANDS) |        |
| Weighted average number of common shares outstanding during the period used to compute basic earnings per share..... | 20,779         | 21,840 |
| Incremental common shares attributable to exercise of outstanding options and warrants.....                          | 1,659          | 2,010  |
| Weighted average number of common shares used to compute diluted earnings per share.....                             | 22,438         | 23,850 |

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CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES  
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(7) INCOME TAXES

In July 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109" ("FIN 48"), which clarifies the accounting and disclosure for uncertainty in tax positions, as defined. FIN 48 seeks to reduce the diversity in practice associated with certain aspects of the recognition and measurement related to accounting for income taxes. We are subject to the provisions of FIN 48 as of January 1, 2007, and have analyzed filing positions in all of the federal and state jurisdictions. As a result of adoption, we recognized a charge of approximately \$1.1 million to the January 1, 2007 retained earnings balance. As of the date of adoption and after the impact of recognizing the increase in liability noted above, our unrecognized tax benefits totaled \$9.8 million. Included in the balance at January 1, 2007, are \$1.2 million of tax positions, the disallowance of which would not affect the annual effective income tax rate.

During the nine months ended September 30, 2007 the Company determined that deferred tax assets totaling approximately \$9.4 million, which were subject to a 100% valuation allowance at December 31, 2006, were permanently not available for future utilization. As a result, the deferred tax assets and the related valuation allowance were adjusted with no impact on the net deferred tax assets recorded or to the provision for income taxes.

We file numerous consolidated and separate income tax returns in the United States Federal jurisdiction and in many state jurisdictions. With few exceptions, we are no longer subject to US Federal income tax examinations for years before 2003 and are no longer subject to state and local income tax examinations by tax authorities for years before 2002.

We have subsidiaries in various states that are currently under audit for years ranging from 1998 through 2005. To date, no material adjustments have been proposed as a result of these audits.

We recognized potential interest and penalties related to unrecognized tax benefits in income tax expense. In conjunction with the adoption of FIN 48, we recognized approximately \$230,000 for the payment of interest and penalties at January 1, 2007 which is included as a component of the \$9.8 million

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unrecognized tax benefit noted above. During the nine months ended September 30, 2007, we did not recognize a significant amount in potential interest and penalties. To the extent interest and penalties are not assessed with respect to uncertain tax positions, amounts accrued will be reduced and reflected as a reduction of the overall income tax provision.

We do not anticipate that total unrecognized tax benefits will significantly change due to the settlement of audits and the expiration of statute of limitations prior to September 30, 2008.

### (8) LEGAL PROCEEDINGS

STANWICH LITIGATION. We were for some time a defendant in a class action (the "Stanwich Case") brought in the California Superior Court, Los Angeles County. The original plaintiffs in that case were persons entitled to receive regular payments (the "Settlement Payments") under out-of-court settlements reached with third party defendants. Stanwich Financial Services Corp. ("Stanwich"), 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 June 2001 filed for reorganization under the Bankruptcy Code, in the federal Bankruptcy Court of Connecticut. At December 31, 2004, we were a defendant only in a cross-claim brought by one of the other defendants in the case, Bankers Trust Company, which asserted a claim of contractual indemnity against us.

We subsequently settled the cross-claim of Bankers Trust by payment of \$3.24 million, on or about February 8, 2006. Pursuant to that settlement, the court has dismissed the cross-claim, with prejudice. The amount paid by us was accrued for and included in accounts payable and accrued expenses in our balance sheet as of December 31, 2004.

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

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. Each of these actions in the court in Rhode Island is stayed, awaiting resolution of an adversary action brought against Mr. Pardee in the bankruptcy court, which is hearing the bankruptcy of Stanwich.

We had reached an agreement in principle with the representative of creditors in the Stanwich bankruptcy to resolve the adversary action, performance of which is now in doubt. Under the agreement in principle, CPS was to pay the bankruptcy estate \$625,000 and abandon its claims against the estate, while the estate would abandon its adversary action against Mr. Pardee. CPS expected that the agreement would result in (i) limitation of its exposure to Mr. Pardee to no more than some portion of his attorneys fees incurred and (ii) the stays in Rhode Island being lifted, causing those cases to become active again. Approval of the bankruptcy court was required. Mr. Pardee objected to the settlement, and the bankruptcy court on October 26, 2007 sustained his objection. As of the date of filing this report, we are uncertain as to (i) whether the ruling of the bankruptcy court may be reversed on appeal, (ii) whether we may be able to reach a substantively similar agreement that can be approved, or (iii) whether the

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estate will proceed with its claims against Mr. Pardee. There can be no assurance as to the ultimate outcome of these matters.

The reader should consider that any adverse judgment against us in these cases 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.

OTHER LITIGATION. On June 2, 2004, Delmar Coleman filed a lawsuit in the circuit court of Tuscaloosa, Alabama, which alleged that plaintiff Coleman was harmed by an alleged failure to refer, in the notice given after repossession of her vehicle, to the right to purchase the vehicle by tender of the full amount owed under the retail installment contract. Plaintiff sought damages in an unspecified amount, on behalf of a purported nationwide class. We removed the case to federal bankruptcy court, and filed a motion for summary judgment as part of our adversary proceeding against the plaintiff in the bankruptcy court. The federal bankruptcy court granted the plaintiff's motion to send the matter back to Alabama state court. We appealed the ruling, and the federal district court, in which the appeal was heard, ordered the bankruptcy court to decide whether the plaintiff had standing to pursue her claims, and, if standing were found, to reconsider its remand decision. The bankruptcy court in May 2007 dismissed the lawsuit with prejudice.

In June 2004, Plaintiff Jeremy Henry filed a lawsuit against us in the California Superior Court, San Diego County, alleging improper practices related to the notice given after repossession of a vehicle that he purchased. Plaintiff's motion for a certification of a class has been denied, and that denial has been affirmed by the California Court of Appeal.

In August and September 2006, two plaintiffs represented by the same law firm filed substantially identical lawsuits in the federal district court for the northern district of Illinois, each of which purports to be a class action, and each of which alleged that we improperly accessed consumer credit information. We have settled both of these cases.

In December 2006 an individual resident of Ohio, Agborebot Bate-Eya, filed a purported class counterclaim to a collection lawsuit brought by SeaWest Financial Corp. ("SeaWest") in Ohio state court. The counterclaim alleged that a form notice sent by SeaWest to counterplaintiff in December 2000, and used then and at other times, was not compliant with Ohio law. In August 2007, the counterplaintiff added us as an additional defendant, noting that we in April 2004 had purchased from SeaWest a number of consumer receivables, including that of the counterplaintiff. We have filed a motion to dismiss the counterclaim, and believe that our no more than tenuous connection to the counterplaintiff will protect us from any material liability or expense. There can be no assurance, however, as to the outcome of contested litigation, including this case.

We have recorded a liability as of September 30, 2007 that we believe represents a sufficient 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.



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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.

### (9) EMPLOYEE BENEFITS

We sponsor the MFN Financial Corporation Benefit Plan ("the Plan"). Plan benefits were frozen September 30, 2001. The table below sets forth the Plan's net periodic benefit cost for the nine-month periods ended September 30, 2007 and 2006.

|   | THREE MONTHS ENDED<br>SEPTEMBER 30, |         | NINE MONTHS<br>SEPTEMBER |       |
|---|-------------------------------------|---------|--------------------------|-------|
|   | 2007                                | 2006    | 2007                     |       |
|   | (IN THOUSANDS)                      |         | (IN THOUSAN              |       |
| Components of net periodic cost (benefit)       |                                     |         |                          |       |
| Service cost.....                               | \$ -                                | \$ -    | \$ -                     | \$ -  |
| Interest Cost.....                              | 223                                 | 219     | 669                      |       |
| Expected return on assets.....                  | (327)                               | (287)   | (982)                    |       |
| Amortization of transition (asset)/obligation.. | (3)                                 | (3)     | (8)                      |       |
| Amortization of net (gain) / loss.....          | 20                                  | 42      | 59                       |       |
|   | -----                               | -----   | -----                    | ----- |
| Net periodic cost (benefit).....                | \$ (87)                             | \$ (29) | \$ (262)                 | \$    |

We made contributions to the Plan in the amount of \$200,000 for the nine-months ended September 30, 2007. We previously disclosed in our Financial Statements for the year ended December 31, 2006 that we did not anticipate making any contributions to the plan during 2007. We presently anticipate that no additional contributions will be made during the remainder of 2007.

### (10) COMPREHENSIVE INCOME

The components of comprehensive income are as follows:

|  | THREE MONTHS ENDED<br>SEPTEMBER 30, |          | NINE MONTHS<br>SEPTEMBER |       |
|--|-------------------------------------|----------|--------------------------|-------|
|  | 2007                                | 2006     | 2007                     |       |
|  | (IN THOUSANDS)                      |          | (IN THOUSAN              |       |
| Net income .....                           | \$ 3,677                            | \$ 4,265 | \$ 10,396                | \$    |
| Minimum pension liability, net of tax..... | -                                   | -        | -                        |       |
|  | -----                               | -----    | -----                    | ----- |
| Comprehensive income .....                 | \$ 3,677                            | \$ 4,265 | \$ 10,396                | \$    |

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### OVERVIEW

We are a specialty finance company engaged in purchasing and servicing new and used retail automobile contracts originated primarily by franchised automobile dealerships and to a lesser extent by select independent dealers of used automobiles in the United States. We serve as an alternative source of financing for dealers, facilitating sales to sub-prime customers, who have limited credit history, low income or past credit problems and who otherwise might not be able to obtain financing from traditional sources. We do not currently lend money directly to consumers but, rather, purchase automobile contracts from dealers under several different financing programs. In addition to our purchases of installment contracts from dealers, since October 2006 we have purchased an immaterial number of vehicle purchase money loans, evidenced by promissory notes and security agreements. A non-affiliated lender originated all such loans directly to vehicle purchasers, and sold the loans to us. We plan to begin financing vehicle purchases by direct loans to consumers in 2007, on terms similar to those that we offer through dealers, though without a down payment requirement. There can be no assurance as to the extent to which we will in fact make any such loans, nor as to their future performance. We are headquartered in Irvine, California and have three additional strategically located servicing branches in Virginia, Florida and Illinois.

On March 8, 2002, we acquired MFN Financial Corporation and its subsidiaries in a merger. On May 20, 2003, we acquired TFC Enterprises, Inc. and its subsidiaries in a second merger. Each merger was accounted for as a purchase. MFN Financial Corporation and its subsidiaries and TFC Enterprises, Inc. and its subsidiaries were engaged in businesses similar to ours: buying automobile contracts from dealers and servicing those automobile contracts. MFN Financial Corporation and its subsidiaries ceased acquiring automobile contracts in May 2002; TFC continues to acquire automobile contracts under its "TFC programs," which provide financing for vehicle purchases exclusively by members of the United States Armed Forces.

On April 2, 2004, we purchased a portfolio of automobile contracts and certain other assets from SeaWest Financial Corporation and its subsidiaries. In addition, we were named the successor servicer of three term securitization transactions originally sponsored by SeaWest. We do not intend to offer financing programs similar to those previously offered by SeaWest.

From inception through June 2003, we generated revenue primarily from the gains recognized on the sale or securitization of automobile contracts, servicing fees earned on automobile contracts sold, interest earned on residual interests retained in securitizations, and interest earned on finance receivables. Since July 2003, we have not recognized any gains from the sale of automobile contracts. Instead, since July 2003 our revenues have been derived from interest on finance receivables (for automobile contracts purchased since July 2003) and to a lesser degree from servicing fees and interest earned on residual interests in securitizations (for automobile contracts purchased prior to July 2003).

### 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 our 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.

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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.

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When structured to be treated as a sale for accounting purposes, the assets and liabilities of the special-purpose subsidiary are not consolidated with us. Accordingly, the transaction removes the sold automobile contracts from our consolidated balance sheet, the related debt does not appear as our debt, and our consolidated balance sheet shows, as an asset, a retained residual interest in the sold automobile contracts. The residual interest represents the discounted value of what we expect will be the excess of future collections on the automobile contracts over principal and interest due on the asset-backed securities. That residual interest appears on our consolidated balance sheet as "residual interest in securitizations," and the determination of its value is dependent on our estimates of the future performance of the sold automobile contracts.

### CHANGE IN POLICY

Beginning in the third quarter of 2003, we began to structure our securitization transactions so that they would be treated for financial accounting purposes as secured financings, rather than as sales. All subsequent securitizations of automobile contracts have been so structured. Prior to the third quarter of 2003, we had structured our securitization transactions to be treated as sales of automobile contracts for financial accounting purposes. In our acquisitions of MFN and TFC, we acquired automobile contracts that these companies had previously securitized in securitization transactions that were treated as secured financings for financial accounting purposes.

### CREDIT RISK RETAINED

Whether a sale of automobile contracts in connection with a securitization or warehouse credit facility is treated as a secured financing or as a sale for financial accounting purposes, the related special-purpose subsidiary may be unable to release excess cash to us if the credit performance of the related automobile contracts falls short of pre-determined standards. Such releases represent a material portion of the cash that we use to fund our operations. An unexpected deterioration in the performance of such automobile contracts could therefore have a material adverse effect on both our liquidity and our results of operations, regardless of whether such automobile contracts are treated for financial accounting purposes as having been sold or as having been financed. For estimation of the magnitude of such risk, it may be appropriate to look to the size of our "managed portfolio," which represents both financed and sold automobile contracts as to which such credit risk is retained. Our managed portfolio as of September 30, 2007 was approximately \$2,053.1 million (this amount includes \$776,000 of automobile contracts securitized by SeaWest, on which we earn only servicing fees and have no credit risk).

### RESULTS OF OPERATIONS

### EFFECTS OF CHANGE IN SECURITIZATION STRUCTURE

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Our decision in the third quarter 2003 to structure securitization transactions as secured financings for financial accounting purposes, rather than as sales, has affected and will affect the way in which the transactions are reported. The major effects are these: (i) the automobile contracts are shown as assets on our balance sheet; (ii) the debt issued in the transactions is shown as indebtedness; (iii) cash deposited in the spread accounts to enhance the credit of the securitization transactions is shown as "Restricted cash and equivalents" on our balance sheet; (iv) cash collected from automobile purchasers and other sources related to the automobile contracts prior to making the required payments under the securitization agreements is also shown as "Restricted cash and equivalents" on our balance sheet; (v) the servicing fee that we receive in connection with such contracts is recorded as a portion of the interest earned on such contracts in our statements of operations; (vi) we have initially and periodically recorded as expense a provision for estimated credit losses on the contracts in our statements of operations; and (vii) portions of scheduled payments on the contracts and on the debt issued in the transactions representing interest are recorded as interest income and expense, respectively, in our statements of operations.

These changes collectively represent a deferral of revenue and acceleration of expenses, and thus a more conservative approach to accounting for our operations compared to the previous securitization transactions, which were accounted for as sales at the consummation of the transaction. As a result of the changes, we initially reported lower earnings than we would have reported if we had continued to structure our transactions to require recognition of gain on sale. It should also be noted that growth in our portfolio of receivables resulted in an increase in expenses in the form of provision for credit losses, and initially had a negative effect on net earnings. Our cash availability and cash requirements should be unaffected by the change in structure.

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Since the third quarter 2003, we have conducted 22 term securitizations. Of these 22, 17 were 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. We repaid the debt from the March 2004 transaction in August 2006 and we repaid the debt from the November 2005 transaction in May 2007. In September 2004, we completed a securitization of automobile contracts purchased in the SeaWest asset acquisition and under our TFC programs. In December 2005 and again in 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. All such securitizations since the third quarter of 2003 have been structured as secured financings.

### COMPARISON OF OPERATING RESULTS FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2007 WITH THE THREE MONTHS ENDED SEPTEMBER 30, 2006

REVENUES. During the three months ended September 30, 2007, revenues were \$102.8 million, an increase of \$29.0 million, or 39.4%, from the prior year period revenue of \$73.7 million. The primary reason for the increase in revenues is an increase in interest income. Interest income for the three months ended September 30, 2007 increased \$26.8 million, or 37.9%, to \$97.4 million from \$70.6 million in the prior year period. The primary reason for the increase in interest income is the increase in finance receivables held by consolidated subsidiaries.

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Servicing fees totaling \$274,000 in the three months ended September 30, 2007 decreased \$359,000, or 56.7%, from \$633,000 in the same period a year earlier. The decrease in servicing fees is the result of the change in securitization structure and the decline in our managed portfolio held by non-consolidated subsidiaries, and also by the decline in the Seawest Third Party Portfolio. We expect to continue to structure future securitizations as secured financings. As a result, our managed portfolio held by non-consolidated subsidiaries will continue to decline in future periods, and servicing fee revenue is anticipated to decline proportionately. As of September 30, 2007 and 2006, our managed portfolio owned by consolidated vs. non-consolidated subsidiaries and other third parties was as follows:

|   | SEPTEMBER 30, 2007 |        | SEPTEMBER 30, 2006 |   |
|---|--------------------|--------|--------------------|---|
|   | AMOUNT             | %      | AMOUNT             | % |
| (\$ IN MILLIONS)                            |                    |        |                    |   |
| Total Managed Portfolio                     |                    |        |                    |   |
| Owned by Consolidated Subsidiaries.....     | \$ 2,052.4         | 100.0% | \$ 1,424.2         |   |
| Owned by Non-Consolidated Subsidiaries..... | -                  | 0.0%   | 50.6               |   |
| SeaWest Third Party Portfolio.....          | 0.7                | 0.0%   | 5.9                |   |
| Total.....                                  | \$ 2,053.1         | 100.0% | \$ 1,480.7         |   |

At September 30, 2007, we were generating income and fees on a managed portfolio with an outstanding principal balance of \$2,053.1 million (this amount includes \$776,000 of automobile contracts securitized by SeaWest, on which we earn only servicing fees), compared to a managed portfolio with an outstanding principal balance of \$1,480.7 million as of September 30, 2006. As the portfolios of automobile contracts acquired in the MFN, TFC and SeaWest transactions decrease, the portfolio of automobile contracts that we have purchased directly from automobile dealers continues to expand. At September 30, 2007 and 2006, the managed portfolio composition was as follows:

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|                                    | SEPTEMBER 30, 2007 |        | SEPTEMBER 30, 2006 |   |
|------------------------------------|--------------------|--------|--------------------|---|
|                                    | AMOUNT             | %      | AMOUNT             | % |
| (\$ IN MILLIONS)                   |                    |        |                    |   |
| Originating Entity                 |                    |        |                    |   |
| CPS.....                           | \$ 1,987.7         | 96.8%  | \$ 1,406.7         |   |
| TFC.....                           | 63.1               | 3.1%   | 61.4               |   |
| MFN.....                           | 0.2                | 0.0%   | 0.4                |   |
| SeaWest.....                       | 1.4                | 0.1%   | 6.3                |   |
| SeaWest Third Party Portfolio..... | 0.7                | 0.0%   | 5.9                |   |
| Total.....                         | \$ 2,053.1         | 100.0% | \$ 1,480.7         |   |

Other income increased \$2.6 million, or 105.9%, to \$5.1 million in the three-month period ended September 30, 2007 from \$2.5 million during the same period a year earlier. Other income includes \$1.2 million resulting from an increase in the carrying value of our residual interest in securitizations. The

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carrying value was increased primarily as a result of the underlying receivables having incurred fewer losses than we had previously estimated. Other income was also impacted by decreases in recoveries on MFN and certain other automobile contracts compared to the same period of the prior year, increases in convenience fees charged to obligors for certain transaction types, recoveries on certain SeaWest receivables and increased revenue on our direct mail services. Direct mail services are provided to our dealers and consist of customized solicitations targeted to prospective vehicle purchasers, in proximity to the dealer, who appear to meet our credit criteria.

EXPENSES. Our operating expenses consist primarily of provisions for credit losses, interest expense, employee costs and general and administrative expenses. Provisions 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 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 warrants and 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 primarily of facilities expenses, telephone and other communication services, credit services, computer services, professional services, marketing and advertising expenses, and depreciation and amortization.

Total operating expenses were \$96.4 million for the three months ended September 30, 2007, compared to \$69.5 million for the same period a year earlier, an increase of \$26.9 million, or 38.8%. The increase is primarily due to increases in provision for credit losses and interest expense, which increased by \$12.3 million and \$11.3 million, or 51.0% and 45.1%, respectively. Both interest expense and provision for credit losses are directly affected by the growth in our portfolio of automobile contracts held by consolidated affiliates. During the three-month period ended September 30, 2007, we purchased 22,012 automobile contracts aggregating \$340.2 million, compared to 16,541 automobile contracts aggregating \$254.4 million in the same period of the prior year. At September 30, 2007, we were earning interest and providing for credit losses on a portfolio with an outstanding principal balance of \$2,052.4 million compared to a portfolio with an outstanding principal balance of \$1,424.2 million as of September 30, 2006. We have increased contract purchases through our continued efforts of adding marketing representatives, expanding into new geographic territories and increasing penetration of existing dealers through an emphasis on service.

Employee costs for the three months ended September 30, 2007 increased by \$2.3 million, or 24.7%, to \$11.6 million from the prior year period of \$9.3 million. The increase in employee costs is the result of additions to our staff, generally throughout all areas of the Company, to accommodate greater volumes of contract purchases and the resulting higher balance of our managed portfolio. As of September 30, 2007 we had 938 employees compared to 705 employees at September 30, 2006. In the 2007 period, employee costs represented 12.0% of total operating expenses compared to 13.4% of total operating expenses in the prior year period. The decrease in employee costs as a percentage of total operating expenses reflects the higher total of operating expenses, primarily a result of the increased provision for credit losses and interest expense.

General and administrative expenses increased by \$176,000, or 2.9%, to \$6.3 million and represented 6.6% of total operating expenses in the three-month period ending September 30, 2007, as compared to \$6.2 million in the prior year period when general and administrative expenses represented 8.9% of total operating expenses. The increase is attributable to the increase in volume of our finance receivable purchases and the corresponding increase in our managed portfolio. The decrease as a percentage of total operating expenses reflects the higher operating expenses primarily a result of the provision for credit losses and interest expense.

Interest expense for the three-month period ended September 30, 2007 increased \$11.3 million, or 45.1%, to \$36.4 million, compared to \$25.0 million in the same period of the previous year. The increase is primarily the result of increases in the amount of securitization trust debt on our balance sheet, increased use of our warehouse lending facilities to accommodate increases in the volume of our finance receivables purchases and a gradual increase in market rates. Interest expense on securitization debt and warehouse facilities increased by \$9.2 million and \$1.2 million, respectively in the three-month period ended September 30, 2007 compared to the prior year period. We also experienced a decrease of \$15,000 in interest on subordinated debt and an increase of \$909,000 on residual interest expense from the 2006 to the 2007 period.

Marketing expenses consist primarily of commission-based compensation paid to our employee marketing representatives and increased by \$1.1 million, or 31.5%, to \$4.8 million, compared to \$3.6 million in the same period of the previous year, and represented 4.9% of total operating expenses. The increase is primarily due to the increase in automobile contracts we purchased during the three months ended September 30, 2007 as compared to the prior year period.

Occupancy expenses decreased slightly to \$949,000 from \$1.1 million the previous year and represented 1.1% of total operating expenses.

Depreciation and amortization expenses decreased by \$76,000, or 37.1%, to \$128,000 from \$204,000 in the same period of the previous year.

#### COMPARISON OF OPERATING RESULTS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2007 WITH THE NINE MONTHS ENDED SEPTEMBER 30, 2006

REVENUES. During the nine months ended September 30, 2007, revenues were \$285.0 million, an increase of \$86.1 million, or 43.3%, from the prior year period revenue of \$198.9 million. The primary reason for the increase in revenues is an increase in interest income. Interest income for the nine months ended September 30, 2007 increased \$79.2 million, or 42.1%, to \$267.4 million from \$188.2 million in the prior year period. The primary reason for the increase in interest income is the increase in finance receivables held by consolidated subsidiaries.

Servicing fees totaling \$669,000 in the nine months ended September 30, 2007 decreased \$1.8 million, or 72.5%, from \$2.4 million in the same period a year earlier. The decrease in servicing fees is the result of the change in securitization structure and the decline in our managed portfolio held by non-consolidated subsidiaries, and also by the decline in the Seawest Third Party Portfolio. As a result of our plans to structure future securitizations as secured financings, our managed portfolio held by non-consolidated subsidiaries will continue to decline in future periods, and servicing fee revenue is anticipated to decline proportionately.

At September 30, 2007, we were generating income and fees on a managed portfolio

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with an outstanding principal balance of \$2,053.1 million (this amount includes \$776,000 of automobile contracts securitized by SeaWest, on which we earn only servicing fees), compared to a managed portfolio with an outstanding principal balance of \$1,480.7 million as of September 30, 2006. As the portfolios of automobile contracts acquired in the MFN, TFC and SeaWest transactions decrease, the portfolio of automobile contracts that we purchased directly from automobile dealers continues to expand.

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Other income increased \$8.7 million, or 104.0%, to \$17.0 million in the nine-month period ended September 30, 2007 from \$8.3 million during the same period a year earlier. Other income includes \$4.8 million resulting from an increase in the carrying value of our residual interest in securitizations. The carrying value was increased primarily as a result of the underlying receivables having incurred fewer losses than we had previously estimated. Other income also includes \$1.7 million from the sale of certain charged off receivables. The charged off receivables were predominately from the acquisitions of MFN, TFC and SeaWest, but also included some receivables that we had previously repurchased from securitizations sponsored by non-consolidated subsidiaries. Other income was also impacted by decreases in recoveries on MFN and certain other automobile contracts compared to the same period of the prior year, increases in convenience fees charged to obligors for certain transaction types, recoveries on certain SeaWest receivables and increased revenue on our direct mail services. Direct mail services are provided to our dealers and consist of customized solicitations targeted to prospective vehicle purchasers, in proximity to the dealer, who appear to meet our credit criteria.

EXPENSES. Our operating expenses consist primarily of provisions for credit losses, interest expense, employee costs and general and administrative expenses. Provisions 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 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 warrants and 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 primarily of facilities expenses, telephone and other communication services, credit services, computer services, professional services, marketing and advertising expenses, and depreciation and amortization.

Total operating expenses were \$267.1 million for the nine months ended September 30, 2007, compared to \$190.3 million for the same period a year earlier, an increase of \$76.8 million, or 40.3%. The increase is primarily due to increases in provision for credit losses and interest expense, which increased by \$33.1 million and \$34.2 million, or 50.7% and 52.3%, respectively. Both interest expense and provision for credit losses are directly affected by the growth in our portfolio of automobile contracts held by consolidated affiliates. During the nine-month period ended September 30, 2007, we purchased 65,909 automobile contracts aggregating \$1,016.5 million, compared to 50,893 automobile contracts aggregating \$777.7 million in the same period of the prior year. At September



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30, 2007, we were earning interest and providing for credit losses on a portfolio with an outstanding principal balance of \$2,052.4 million compared to a portfolio with an outstanding principal balance of \$1,424.2 million as of September 30, 2006. We have increased contract purchases through our continued efforts of adding marketing representatives, expanding into new geographic territories and increasing penetration of existing dealers through an emphasis on service.

Employee costs for the nine months ended September 30, 2007 increased by \$5.4 million, or 18.9%, to \$33.7 million from the prior year period of \$28.3 million. The increase in employee costs is the result of additions to our staff, generally throughout all areas of the Company, to accommodate greater volumes of contract purchases and the resulting higher balance of our managed portfolio. As of September 30, 2007 we had 938 employees compared to 705 employees at September 30, 2006. In the 2007 period, employee costs represented 12.6% of total operating expenses compared to 14.9% of total operating expenses in the prior year period. The decrease in employee costs as a percentage of total operating expenses reflects the higher total of operating expenses, primarily a result of the increased provision for credit losses and interest expense.

General and administrative expenses increased by \$1.4 million, or 8.5%, to \$18.4 million and represented 6.9% of total operating expenses in the nine-month period ending September 30, 2007, as compared to \$16.9 million in the prior year period when general and administrative expenses represented 8.9% of total operating expenses. The increase is attributable to the increase volume of our finance receivable purchases and the corresponding increase in our managed portfolio. The decrease as a percentage of total operating expenses reflects the higher operating expenses primarily a result of the provision for credit losses and interest expense.

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Interest expense for the nine-month period ended September 30, 2007 increased \$34.2 million, or 52.3%, to \$99.6 million, compared to \$65.4 million in the same period of the previous year. The increase is primarily the result of increases in the amount of securitization trust debt on our balance sheet, increased use of our warehouse lending facilities to accommodate increases in the volume of our finance receivables purchases and a gradual increase in market rates. Interest expense on securitization debt and warehouse facilities increased by \$29.9 million and \$4.3 million, respectively in the nine-month period ended September 30, 2007 compared to the prior year period. We also experienced an increase of \$206,000 in interest on subordinated debt and a decrease of \$199,000 on residual interest expense from the 2006 to the 2007 period.

Marketing expenses consist primarily of commission-based compensation paid to our employee marketing representatives and increased by \$2.9 million, or 27.4%, to \$13.6 million, compared to \$10.7 million in the same period of the previous year, and represented 5.1% of total operating expenses. The increase is primarily due to the increase in automobile contracts we purchased during the nine months ended September 30, 2007 as compared to the prior year period.

Occupancy expenses were \$2.8 million for the nine months ended September 30, 2007, representing 1.1% of total operating expenses and were \$105,000 less than the prior year period.

Depreciation and amortization expenses decreased by \$178,000, or 29.8%, to \$418,000 from \$596,000 in the same period of the previous year.

CREDIT EXPERIENCE

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Our financial results are dependent on the performance of the automobile contracts in which we retain an ownership interest. The table below documents the delinquency, repossession and net credit loss experience of all automobile contracts that we were servicing (excluding automobile contracts from the SeaWest Third Party Portfolio) as of the respective dates shown. Credit experience for CPS, MFN (since the date of the MFN transaction), TFC (since the date of the TFC transaction) and SeaWest (since the date of the SeaWest transaction) is shown on a combined basis in the table below.

### DELINQUENCY EXPERIENCE (1) CPS, MFN, TFC AND SEAWEST COMBINED

|  | SEPTEMBER 30, 2007     |              | SEPTEMBER 30,          |       |
|--|------------------------|--------------|------------------------|-------|
|  | NUMBER OF<br>CONTRACTS | AMOUNT       | NUMBER OF<br>CONTRACTS | A     |
|  |                        |              | (DOLLARS IN THO        |       |
| <b>DELINQUENCY EXPERIENCE</b>  |                        |              |                        |       |
| Gross servicing portfolio (1).....   | 161,984                | \$ 2,055,962 | 120,328                | \$ 1, |
| Period of delinquency (2)  |                        |              |                        |       |
| 31-60 days.....  | 4,358                  | 50,691       | 2,842                  |       |
| 61-90 days.....  | 2,205                  | 25,691       | 1,281                  |       |
| 91+ days.....  | 1,678                  | 18,469       | 1,021                  |       |
| Total delinquencies (2).....   | 8,241                  | 94,851       | 5,144                  |       |
| Amount in repossession (3).....  | 2,569                  | 29,748       | 1,770                  |       |
| Total delinquencies and amount in<br>repossession (2).....   | 10,810                 | \$ 124,599   | 6,914                  | \$    |
| Delinquencies as a percentage of gross<br>servicing portfolio.....                                 | 5.1%                   | 4.6%         | 4.3%                   |       |
| Total delinquencies and amount in repossession<br>as a percentage of gross servicing portfolio.... | 6.7%                   | 6.1%         | 5.7%                   |       |

(1) ALL AMOUNTS AND PERCENTAGES ARE BASED ON THE AMOUNT REMAINING TO BE REPAYED ON EACH AUTOMOBILE CONTRACT, INCLUDING, FOR PRE-COMPUTED AUTOMOBILE CONTRACTS, ANY UNEARNED INTEREST. THE INFORMATION IN THE TABLE REPRESENTS THE GROSS PRINCIPAL AMOUNT OF ALL AUTOMOBILE CONTRACTS PURCHASED BY US, INCLUDING AUTOMOBILE CONTRACTS SUBSEQUENTLY SOLD BY US IN SECURITIZATION TRANSACTIONS THAT WE CONTINUE TO SERVICE. THE TABLE DOES NOT INCLUDE AUTOMOBILE CONTRACTS FROM THE SEAWEST THIRD PARTY PORTFOLIO.

(2) WE CONSIDER AN AUTOMOBILE CONTRACT DELINQUENT WHEN AN OBLIGOR FAILS TO MAKE AT LEAST 90% OF A CONTRACTUALLY DUE PAYMENT BY THE FOLLOWING DUE DATE, WHICH DATE MAY HAVE BEEN EXTENDED WITHIN LIMITS SPECIFIED IN THE SERVICING AGREEMENTS. THE PERIOD OF DELINQUENCY IS BASED ON THE NUMBER OF DAYS PAYMENTS ARE CONTRACTUALLY PAST DUE. AUTOMOBILE CONTRACTS LESS THAN 31 DAYS DELINQUENT ARE NOT INCLUDED.

(3) AMOUNT IN REPOSSESSION REPRESENTS FINANCED VEHICLES THAT HAVE BEEN REPOSSESSED BUT NOT YET LIQUIDATED.

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NET CHARGE-OFF EXPERIENCE (1)  
CPS, MFN, TFC AND SEAWEST COMBINED

|   | SEPTEMBER 30,<br>2007  | SEPTEMBER 30,<br>2006 | DECEMBER 31,<br>2006 |
|---|------------------------|-----------------------|----------------------|
|   | -----                  |                       |                      |
|   | (DOLLARS IN THOUSANDS) |                       |                      |
| Average servicing portfolio outstanding.....  | \$ 1,837,634           | \$ 1,312,348          | \$ 1,367,9           |
| Annualized net charge-offs as a percentage of<br>average servicing portfolio (2)..... | 5.0%                   | 4.0%                  | 4                    |

(1) ALL AMOUNTS AND PERCENTAGES ARE BASED ON THE PRINCIPAL AMOUNT SCHEDULED TO BE PAID ON EACH AUTOMOBILE CONTRACT, NET OF UNEARNED INCOME ON PRE-COMPUTED AUTOMOBILE CONTRACTS. THE INFORMATION IN THE TABLE REPRESENTS ALL AUTOMOBILE CONTRACTS SERVICED BY US (EXCLUDING AUTOMOBILE CONTRACTS FROM THE SEAWEST THIRD PARTY PORTFOLIO). (2) NET CHARGE-OFFS INCLUDE THE REMAINING PRINCIPAL BALANCE, AFTER THE APPLICATION OF THE NET PROCEEDS FROM THE LIQUIDATION OF THE VEHICLE (EXCLUDING ACCRUED AND UNPAID INTEREST) AND AMOUNTS COLLECTED SUBSEQUENT TO THE DATE OF CHARGE-OFF, INCLUDING SOME RECOVERIES WHICH HAVE BEEN CLASSIFIED AS OTHER INCOME IN THE ACCOMPANYING INTERIM FINANCIAL STATEMENTS. SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006 PERCENTAGE REPRESENTS NINE MONTHS ENDED SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006 ANNUALIZED. DECEMBER 31, 2006 REPRESENTS 12 MONTHS ENDED DECEMBER 31, 2006.

LIQUIDITY AND CAPITAL RESOURCES

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 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, 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, 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 account), 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.

Net cash provided by operating activities for the nine-month period ended September 30, 2007 was \$52.2 million compared to net cash provided by operating activities for the nine-month period ended September 30, 2006 of 22.9 million. Cash provided by operating activities is affected by our increased net earnings before the significant increase in the provision for credit losses. This impact is somewhat negated by the increase in restricted cash as a result of our pre-funding structure used in the securitization of our finance receivables. The pre-funding structure allows us to issue securitization trust debt approximately

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one month prior to purchasing finance receivables that collateralize the debt. In those cases, certain of the proceeds of the securitization debt are held as restricted cash until such time as the additional collateral is delivered to the related trust.

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Net cash used in investing activities for the nine-month period ended September 30, 2007 and 2006 was \$584.5 million and \$448.7 million, respectively. Cash used in investing activities has primarily related to purchases of automobile contracts less principal amortization on our consolidated portfolio of automobile contracts.

Net cash provided by financing activities for the nine months ended September 30, 2007 and 2006, was \$535.0 million and \$423.3 million, respectively. Cash provided by financing activities is generally related to the issuance of new securitization trust debt. We issued \$1,035.5 million and \$786.1 million of such debt in the nine-month periods ended September 30, 2007 and 2006, respectively. Cash used in financing activities also includes the repayment of securitization trust debt of \$498.2 million and \$356.3 million for the nine-month periods ended September 30, 2007 and 2006, respectively.

We purchase automobile contracts from dealers for a cash price approximating their principal amount, adjusted for an acquisition fee that 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. As of September 30, 2007, we had \$425 million in warehouse credit capacity, in the form of two \$200 million senior facilities and one \$25 million subordinated facility. The subordinated facility, which is used with each of the senior facilities, was established on January 12, 2007 and expires on January 12, 2008. One \$200 million senior facility provides funding for automobile contracts purchased under the TFC programs while both senior facilities provide funding for automobile contracts purchased under the CPS programs.

The first of the two senior warehouse facilities mentioned above is structured to allow us to fund a portion of the purchase price of automobile contracts by drawing against a floating rate variable funding note issued by our consolidated subsidiary Page Three Funding LLC. This facility was established on November 15, 2005, and expires on November 8, 2007, although it is renewable with the mutual agreement of the parties. On November 8, 2006 the facility was increased from \$150 million to \$200 million and the advance was increased to 83% from 80% of eligible contracts, subject to collateral tests and certain other conditions and covenants. On January 12, 2007 the facility was amended to allow for the issuance of subordinated notes and the maximum advance was increased to 93%. Senior notes under this facility accrue interest at a rate of one-month LIBOR plus 2.00% per annum while subordinated notes accrue interest at a rate of one-month LIBOR plus 5.50% per annum. At September 30, 2007, \$59.3 million in senior and subordinated notes were outstanding.

The second of the two senior warehouse facilities is similarly structured to allow us to fund a portion of the purchase price of automobile contracts by drawing against a floating rate variable funding note issued by our consolidated subsidiary Page Funding LLC. This facility was entered into on September 30, 2004. On September 29, 2005 the facility was increased from \$100 million to \$125 million and further amended to provide for funding for automobile contracts

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purchased under the TFC programs. It was increased again to \$200 million on August 31, 2005. Up to 93.0% of the principal balance of automobile contracts may be advanced to us in senior and subordinated notes, subject to collateral tests and certain other conditions and covenants. Senior notes under this facility accrue interest at a rate of one-month LIBOR plus 2.00% per annum while subordinated notes accrue interest at a rate of one-month LIBOR plus 5.50% per annum. This facility was renewed as of September 30, 2007, and now expires on September 30, 2008. At September 30, 2007, \$19.8 million in senior and subordinated notes were outstanding.

The balance under these warehouse facilities generally will increase as we purchase additional automobile contracts, until we effect a securitization utilizing automobile contracts pledged to the warehouse facilities. Proceeds from the securitization are then used to pay down the outstanding balance of the warehouse facilities.

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For the portfolio owned by consolidated subsidiaries, cash released from Trusts and their related spread accounts to us for the nine-month period ended September 30, 2007 and 2006, was \$2.7 million and \$11.1 million, respectively. Changes in the amount of credit enhancement required for term securitization transactions and releases from Trusts and their related spread account are affected by the relative size, seasoning and performance of the various pools of automobile contracts securitized that make up our managed portfolio to which the respective spread account is related. Furthermore, the trend in our recent securitizations has been towards credit enhancements that require a lower proportion of spread account cash and a greater proportion of over-collateralization. This trend has led to significantly lower levels of restricted cash and releases from trusts relative to the size of our managed portfolio.

The acquisition of automobile contracts for subsequent sale in securitization transactions, and the need to fund the 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 advance rate on the warehouse facilities, the required level of initial credit enhancement in securitizations, and the extent to which the previously established Trusts and their related spread account either release cash to us or capture cash from collections on securitized automobile contracts. We are limited in our ability to purchase automobile contracts by our available cash and the capacity of our warehouse facilities. As of September 30, 2007, we had unrestricted cash on hand of \$16.9 million and available capacity from our warehouse credit facilities of \$320.9 million, subject to the availability of suitable automobile contracts to serve as collateral and of sufficient cash to fund the portion of such automobile contracts purchase price not advanced under the warehouse facilities. Our plans to manage our liquidity include the completion of additional term securitizations that may result in additional unrestricted cash through repayment of the warehouse facilities, and matching our levels of automobile contract purchases to our availability of cash. There can be no assurance that we will be able to complete term securitizations on favorable economic terms or that we will be able to complete term securitizations at all. If we are unable to complete such securitizations, interest income and other portfolio related income would decrease.

Our primary means of ensuring that our cash demands do not exceed our cash resources is to match our levels of automobile contract purchases to our availability of cash. Our ability to adjust the quantity of automobile contracts

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that it purchases and securitizes will be subject to general competitive conditions and the continued availability of warehouse credit facilities. There can be no assurance that the desired level of automobile contract acquisition can be maintained or increased. 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 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 note 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.

The terms of the various securitization agreements related to the issuance of the securitization trust debt and the warehouse credit facilities require that certain delinquency and credit loss criteria be met with respect to the collateral pool, and require that we maintain minimum levels of liquidity and net worth and not exceed maximum leverage levels and maximum financial losses. In addition, certain securitization and non-securitization related debt contain cross-default provisions, which would allow certain creditors to declare a default if a default were declared under a different facility. As of September 30, 2007, we were in compliance with all such financial covenants.

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The securitization agreements of our term securitization transactions are terminable by the note insurers in the event of certain defaults by us and under certain other circumstances. Similar termination rights are held by the lenders in the warehouse credit facilities. Were a note insurer (or the lenders in such warehouse facilities) in the future to exercise its option to terminate the securitization agreements, such a termination would have a material adverse effect on our liquidity and results of operations. We continue to receive Servicer extensions on a monthly and/or quarterly basis, pursuant to the securitization agreements.

In our annual report on Form 10-K we identified as one of our capital requirements our obligation to repay \$25.0 million of outstanding senior secured debt by its maturity date of May 31, 2007. In July 2007, we opened a combination term and revolving residual credit facility, and used a portion of our initial draw under that facility to repay our remaining outstanding debt under this obligation, after having been partially repaid and amended with respect to the maturity date during the preceding quarter.

Under this facility, we have used and intend to use eligible residual interests in securitizations as collateral for floating rate borrowings. The amount that may be borrowed is computed using an agreed valuation methodology of the residuals, subject to an overall maximum principal amount of \$120 million that may be borrowed represented by (i) a \$60 million Class A-1 Variable Funding Note (the "Revolving Note"), and (ii) a \$60 million Class A-2 Term Note (the "Term Note"). The facility's revolving feature is to expire by its terms in July 2008. The Term Note has been fully drawn and is due in July 2009.

Our indebtedness under the new facility carries interest rates higher than the weighted average interest rates of the debt it replaces. Accordingly, we anticipate that our interest expense over the next one to two years will

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increase, over and above the increase that would be expected as a result of increases in the amount of securitization trust debt outstanding.

### CRITICAL ACCOUNTING POLICIES

#### (A) ALLOWANCE FOR FINANCE CREDIT LOSSES

In order to estimate an appropriate allowance for losses incurred on finance receivables held on our Unaudited Condensed Consolidated Balance Sheet, we use a loss allowance methodology commonly referred to as "static pooling," which stratifies our finance receivable portfolio into separately identified pools. Using analytical and formula-driven techniques, we estimate an allowance for finance credit losses, which management believes is adequate for probable credit losses that can be reasonably estimated in our portfolio of finance receivable automobile contracts. Provision for losses is charged to our Unaudited Consolidated Statement of Operations. Net losses incurred on finance receivables are charged to the allowance. Management evaluates the adequacy of the allowance by examining current delinquencies, the characteristics of the portfolio and the value of the underlying collateral. As conditions change, our level of provisioning and/or allowance may change as well.

#### (B) CONTRACT ACQUISITION FEES AND ORIGINATIONS COSTS

Upon purchase of a Contract from a Dealer, we generally charge or advance the Dealer an acquisition fee. For Contracts securitized in pools which were structured as sales for financial accounting purposes, the acquisition fees associated with Contract purchases were deferred until the Contracts were securitized, at which time the deferred acquisition fees were recognized as a component of the gain on sale.

For Contracts purchased and securitized in pools which are structured as secured financings for financial accounting purposes, dealer acquisition fees and deferred originations costs are reduced against the carrying value of finance receivables and are accreted into earnings as an adjustment to the yield over the estimated life of the Contract using the interest method.

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#### (C) INCOME TAXES

We and our subsidiaries file consolidated federal income and combined state franchise tax returns. 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 period is not more than likely. In determining the possible realization of deferred tax assets, future taxable income from the following sources are considered: (a) the reversal of taxable temporary differences; (b) future operations exclusive of reversing temporary differences; and (c) tax planning strategies that, if necessary, would be implemented to accelerate taxable income into a period in which net operating losses might otherwise expire.

#### (D) STOCK-BASED COMPENSATION

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Effective January 1, 2006, we adopted Statement of Financial Accounting Standards No. 123(R), "Share-Based Payment, revised 2004" ("SFAS 123R"), prospectively for all option awards granted, modified or settled on or after January 1, 2006, using the modified prospective method. Under this method, we recognize compensation costs in the financial statements for all share-based payments granted subsequent to December 31, 2005 based on the grant date fair value estimated in accordance with the provisions of SFAS 123(R).

In December 2005, the Compensation Committee of the Board of Directors approved accelerated vesting of all the outstanding stock options issued by us. Options to purchase 2,113,998 shares of our common stock, which would otherwise have vested from time to time through 2010, became immediately exercisable as a result of the acceleration of vesting. The decision to accelerate the vesting of the options was made primarily to reduce non-cash compensation expenses that would have been recorded in our income statement in future period upon the adoption of Financial Accounting Standards Board Statement No. 123(R) in January 2006.

For the nine months ended September 30, 2007, we recorded \$785,000 in stock-based compensation costs, resulting from grants of options during the period and vesting of previously granted options. As of September 30, 2007, there were \$4.4 million in unrecognized stock-based compensation costs to be recognized over future periods.

Prior to January 1, 2006, as was permitted by Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" ("SFAS No. 123"), we accounted for stock-based employee compensation plans in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations, whereby stock options are recorded at intrinsic value equal to the excess of the share price over the exercise price at the date of grant.

### FORWARD LOOKING STATEMENTS

This report on Form 10-Q includes certain "forward-looking statements." Forward-looking statements may be identified by the use of words such as "anticipates," "expects," "plans," "estimates," or words of like meaning. Our provision for credit losses is a forward-looking statement, as it is dependent on our estimates as to future chargeoffs and recovery rates. Factors that could affect charge-offs and recovery rates include changes in the general economic climate, which could affect the willingness or ability of obligors to pay pursuant to the terms of automobile contracts, changes in laws respecting consumer finance, which could affect our ability to enforce rights under automobile contracts, and changes in the market for used vehicles, which could affect the levels of recoveries upon sale of repossessed vehicles. Factors that could affect our revenues in the current year include the levels of cash releases from existing pools of automobile contracts, which would affect our ability to purchase automobile contracts, the terms on which we are able to finance such purchases, the willingness of Dealers to sell automobile contracts to us on the terms that we offer, and the terms on which we are able to complete term securitizations once automobile contracts are acquired. Factors that could affect our expenses in the current year include competitive conditions in the market for qualified personnel and interest rates (which affect the rates that we pay on Notes issued in our securitizations). The statements concerning our structuring future securitization transactions as secured financings and the effects of such structures on financial items and on our future profitability also are forward-looking statements. Any change to the structure of our securitization transaction could cause such forward-looking statements not to be accurate. Both the amount of the effect of the change in structure on our profitability and the duration of the period in which our profitability would be affected by the change in securitization structure are estimates. The accuracy



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of such estimates will be affected by the rate at which we purchase and sell automobile contracts, any changes in that rate, the credit performance of such automobile contracts, the financial terms of future securitizations, any changes in such terms over time, and other factors that generally affect our profitability.

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### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

#### INTEREST RATE RISK

We are subject to interest rate risk during the period between when automobile contracts are purchased from Dealers and when such automobile contracts become part of a term securitization. Specifically, the interest rates on the warehouse facilities are adjustable while the interest rates on the automobile contracts are fixed. Historically, our term securitization facilities have had fixed rates of interest. To mitigate some of this risk, we have in the past, and intend to continue to, structure certain of our securitization transactions to include pre-funding structures, in which the amount of Notes issued exceeds the amount of automobile contracts initially sold to the Trusts. In pre-funding, the proceeds from the pre-funded portion are held in an escrow account until we sell the additional automobile contracts to the Trust in amounts up to the balance of the pre-funded escrow account. In pre-funded securitizations, we lock in the borrowing costs with respect to the automobile contracts it subsequently delivers to the Trust. However, we incur an expense in pre-funded securitizations equal to the difference between the money market yields earned on the proceeds held in escrow prior to subsequent delivery of automobile contracts and the interest rate paid on the Notes outstanding, as to the amount of which there can be no assurance.

There have been no material changes in market risks since December 31, 2006.

### ITEM 4. CONTROLS AND PROCEDURES

We maintain a system of internal controls and procedures designed to provide reasonable assurance as to the reliability of our published financial statements and other disclosures included in this report. As of the end of the period covered by this report, we evaluated the effectiveness of the design and operation of such disclosure controls and procedures. Based upon that evaluation, the principal executive officer (Charles E. Bradley, Jr.) and the principal financial officer (Jeffrey P. Fritz) concluded that the disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, material information relating to us that is required to be included in our reports filed under the Securities Exchange Act of 1934. There have been no significant changes in our internal controls over financial reporting during our most recently completed fiscal quarter that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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## PART II -- OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

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The information provided under the caption "Legal Proceedings" in our Annual Report on Form 10-K for the year ended December 31, 2006, is incorporated herein by reference. In addition, the reader should be aware of the following:

Our annual report on Form 10-K disclosed that a hearing to consider a proposed settlement of an adversary action arising out of the bankruptcy of Stanwich Financial Services Corp. would be held in March 2007 in the federal bankruptcy court sitting in Connecticut. The court in October 2007 rejected the settlement. As of the date of filing this report, we are uncertain as to (i) whether the ruling of the bankruptcy court may be reversed on appeal, (ii) whether we may be able to reach a similar agreement that can be approved, or (iii) whether the estate will proceed with its adversary action. There can be no assurance as to the outcome.

Our annual report on Form 10-K also disclosed that the COLEMAN matter, a purported class action arising out of alleged irregularities in the notices we gave following repossessions of vehicles, was pending before the federal bankruptcy court in Alabama. That court has since dismissed with prejudice the claims of the plaintiff Coleman.

Our annual report on Form 10-K also disclosed that in the HENRY matter, a purported class action arising out of alleged irregularities in the notices given following repossessions of vehicles, the plaintiff's appeal of the trial court's denial of a class certification motion was pending before the Court of Appeal of California. That court has since affirmed the denial of class certification. The case continues in the trial court, on an individual basis and not a class basis.

In December 2006 an individual resident of Ohio, Agborebot Bate-Eya, filed a purported class counterclaim to a collection lawsuit brought by SeaWest Financial Corp. ("SeaWest") in Ohio state court. The counterclaim alleged that a form notice sent by SeaWest to counterplaintiff in December 2000, and used then and at other times, was not compliant with Ohio law. In August 2007, the counterplaintiff added us as an additional defendant, noting that we in April 2004 had purchased from SeaWest a number of consumer receivables, including that of the counterplaintiff. We have filed a motion to dismiss the counterclaim, and believe that our no more than tenuous connection to the counterplaintiff will protect us from any material liability or expense. There can be no assurance, however, as to the outcome of contested litigation, including this case.

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.

### ITEM 1A. RISK FACTORS

We remind the reader that risk factors are set forth in Item 1A of our report on Form 10-K, filed with the U.S. Securities and Exchange Commission on March 9, 2007.

### ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

During the three months ended September 30, 2007, we purchased a total of 1,755,251 shares of our common stock, as described in the following table:

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## ISSUER PURCHASES OF EQUITY SECURITIES

| PERIOD (1)      | TOTAL<br>NUMBER OF<br>SHARES<br>PURCHASED | AVERAGE<br>PRICE PAID<br>PER SHARE | TOTAL NUMBER OF<br>SHARES PURCHASED AS<br>PART OF PUBLICLY<br>ANNOUNCED PLANS OR<br>PROGRAMS (2) | APPROXIMATE DOLLAR<br>VALUE OF SHARES THAT<br>MAY YET BE PURCHASED<br>UNDER THE PLANS OR<br>PROGRAMS |
|-----------------|---|------------------------------------|--|--|
| July 2007       | 65,261                                    | \$ 5.96                            | 65,261   | \$ 3,274,68  |
| August 2007 (3) | 1,689,790                                 | 5.01                               | 189,790  | 2,306,12   |
| September 2007  | 200                                       | 5.87                               | 200  | 2,304,94   |
|                 | -----<br>1,755,251<br>=====               | -----<br>\$ 5.05<br>=====          | -----<br>255,251<br>=====  |  |

(1) EACH MONTHLY PERIOD IS THE CALENDAR MONTH.

(2) OUR BOARD OF DIRECTORS IN FEBRUARY 2007 AUTHORIZED THE PURCHASE OF UP TO AN ADDITIONAL \$5 MILLION OF OUR OUTSTANDING SECURITIES.

(3) INCLUDES THE PURCHASE OF 1,500,000 SHARES OF OUR COMMON STOCK FROM LEVINE LEICHTMAN CAPITAL PARTNERS II, L.P. AT A PRICE OF \$5.00 PER SHARE, OUTSIDE OF AND IN ADDITION TO OUR ONGOING REPURCHASE PROGRAMS.

### ITEM 6. EXHIBITS

The Exhibits listed below are filed with this report.

- 4.14 Instruments defining the rights of holders of long-term debt of certain consolidated subsidiaries of the registrant are omitted pursuant to the exclusion set forth in subdivisions (b)(iv)(iii)(A) and (b)(v) of Item 601 of Regulation S-K (17 CFR 229.601). The registrant agrees to provide copies of such instruments to the United States Securities and Exchange Commission upon request.
- 4.25 Indenture dated as of September 1, 2007, respecting notes issued by CPS Auto Receivables Trust 2007-C (exhibit 4.25 to Form 8-K/A filed by the registrant on November 2, 2007)
- 4.26 Sale and Servicing Agreement dated as of September 1, 2007, re CPS Auto Receivables Trust 2007-C (exhibit 4.26 to Form 8-K/A filed by the registrant on November 2, 2007)
- 10.5.3 Amendment dated as of September 30, 2007, to the Third Amended & Restated Sale and Servicing Agreement dated as of February 14, 2007 by and among PFLLC, the registrant and WFBNA (filed herewith)
- 31.1 Rule 13a-14(a) Certification of the Chief Executive Officer of the registrant.
- 31.2 Rule 13a-14(a) Certification of the Chief Financial Officer of the registrant.
- 32 Section 1350 Certifications.\*

\* These Certifications shall not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liability of that section. These Certifications shall not be deemed to be

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incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Exchange Act, except to the extent that the registration statement specifically states that such Certifications are incorporated therein.

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SIGNATURES

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

CONSUMER PORTFOLIO SERVICES, INC.  
(Registrant)

Date: November 5, 2007

By: /s/ CHARLES E. BRADLEY, JR.

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Charles E. Bradley, Jr.  
PRESIDENT AND CHIEF EXECUTIVE OFFICER  
(Principal Executive Officer)

Date: November 5, 2007

By: /s/ JEFFREY P. FRITZ

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Jeffrey P. Fritz  
SENIOR VICE PRESIDENT AND  
CHIEF FINANCIAL OFFICER  
(Principal Financial Officer)

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