ENCORE CAPITAL GROUP INC
Form 10-K
February 14, 2011
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2010 or

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

For the transition period from to .

COMMISSION FILE NUMBER: 000-26489

ENCORE CAPITAL GROUP, INC.

(Exact name of registrant as specified in its charter)

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

(877) 445-4581

(Registrant s telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, $.01 Par Value Per Share	The NASDAQ Stock Market LLC

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No x

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

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

Large accelerated filer ¨	Accelerated filer x	Non-accelerated filer ¨	Smaller reporting company ¨

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

The aggregate market value of the voting stock held by non-affiliates of the registrant totaling 10,975,458 shares was $226,204,189 at June 30, 2010, based on the closing price of the common stock of $20.61 per share on such date, as reported by the NASDAQ Global Select Market.

The number of shares of our Common Stock outstanding at February 1, 2011, was 24,018,538.

Documents Incorporated by Reference

Portions of the registrant s proxy statement in connection with its annual meeting of stockholders to be held in 2011 are incorporated by reference in Items 10, 11, 12, 13, and 14 of Part III of this Annual Report on Form 10-K for the fiscal year ended December 31, 2010.

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PART I

Item 1 Business

An Overview of Our Business

Nature of Business

We are a leader in consumer debt buying and recovery. We purchase portfolios of defaulted consumer receivables at deep discounts to face value and use a variety of operational channels to maximize our collections from these portfolios. We manage our receivables by partnering with individuals as they repay their obligations and work toward financial recovery. Defaulted receivables are consumers unpaid financial commitments to credit originators, including banks, credit unions, consumer finance companies, commercial retailers, auto finance companies, and telecommunication companies, and may also include receivables subject to bankruptcy proceedings, or consumer bankruptcy receivables.

Four competitive, strategic advantages underpin our success and drive our future growth:

- The sophisticated and widespread use of analytics (**Analytic Strength**)
- Broad investments in data and behavioral science (**Consumer Intelligence**)
- Significant cost advantages based on our operations in India, as well as our enterprise-wide, account-level cost database (**Cost Leadership**)
- A demonstrated commitment to conduct business ethically and in ways that support our consumers financial recovery (**Principled Intent**)

Although we have enabled approximately one million consumers to retire a portion of their outstanding debt since 2007, one of the industry s most formidable challenges is that many distressed consumers will never make a payment, much less retire their total obligation. In fact, at the peak of the collection cycle, we generate payments from fewer than one percent of our accounts every month. To address these challenges, we evaluate portfolios of receivables that are available for purchase using robust, account-level valuation methods and we employ a suite of proprietary statistical and behavioral models across the full extent of our operations. We believe these business practices contribute to our ability to value portfolios accurately, avoid buying portfolios that are incompatible with our methods or goals, and align the accounts we purchase with our operational channels to maximize future collections. We also have one of the industry s largest distressed consumer databases containing information regarding approximately 20 million consumer accounts. We believe that our specialized knowledge, along with our investments in data and analytic tools, have enabled us to realize significant returns from the receivables we have acquired. From inception through December 31, 2010, we have invested approximately $1.8 billion to acquire 33.0 million consumer accounts with a face value of approximately $54.7 billion. We maintain strong relationships with many of the largest credit providers in the United States, and believe that we possess one of the industry s best collection staff retention rates.

While seasonality does not have a material impact on our business, collections are generally strongest in our first calendar quarter, slower in the second and third calendar quarters, and slowest in the fourth calendar quarter. Relatively higher collections in the first quarter could result in a lower cost-to-collect ratio compared to the fourth quarter, as our fixed costs would be constant and applied against a larger collection base. The seasonal impact on our business may be influenced by our purchasing levels, the types of portfolios we purchase, and our operating strategies.

In addition, we provide bankruptcy support services to some of the largest companies in the financial services industry through our wholly owned subsidiary, Ascension Capital Group, Inc. (Ascension). Leveraging a proprietary software platform dedicated to bankruptcy servicing, Ascension s operational platform integrates lenders, trustees, and consumers across the bankruptcy lifecycle.

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Investors wishing to obtain more information about us may access our internet site (www.encorecapital.com). The site provides access to relevant investor related information such as Securities and Exchange Commission (SEC) filings, press releases, featured articles, an event calendar, and frequently asked questions. SEC filings are available on the website as soon as reasonably practicable after being filed with, or furnished to, the SEC. The content of the internet site is not incorporated by reference into this Annual Report on Form 10-K. Any materials that the Company filed with the SEC also may be read and copied at the SEC s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC (http://www.sec.gov).

Our Competitive Advantages

Analytic Strength. We believe that success in our business depends on the ability to establish and maintain an information advantage. Leveraging an industry-leading distressed consumer database, our in-house team of statisticians, business analysts, and software programmers have developed, and continually enhance, proprietary behavioral and valuation models, custom software applications, and other business tools that guide our portfolio purchases. Moreover, our collection channels are informed by powerful statistical models specific to each collection activity, and each year we deploy significant capital to purchase credit bureau and customized consumer data that describe demographic, account level, and macroeconomic factors related to credit, savings, and payment behavior.

Consumer Intelligence. At the core of our analytic approach is a focus on understanding, measuring, and predicting distressed consumer behavior. In this effort, we apply tools and methods borrowed from statistics, psychology, economics, and management science across the full extent of our business. During portfolio valuation, we use an internally-developed and proprietary family of statistical models that determines the likelihood and expected amount of payment for each consumer within a portfolio. Subsequently, the expectations for each account are aggregated to arrive at a portfolio-level liquidation solution and a valuation for the entire portfolio is determined. During collections, we apply our willingness-capability framework, which allows us to match our collection approach to an individual consumer s payment behavior.

Cost Leadership. Cost efficiency is central to our collection and purchasing strategies. We experience considerable cost advantages, stemming from our operations in India, our enterprise-wide, activity-level cost database, and the development and implementation of operational models that enhance profitability. We believe that we are the only company in our industry with a successful, late-stage collection platform in India. This cost-saving, first-mover advantage helps to reduce our call center variable cost-to-collect.

Principled Intent. We strive to treat consumers with respect, compassion and integrity. From discounts and payment plans to hardship solutions, we partner with our consumers as they attempt to return to financial health. We are committed to dialogue that is honorable and constructive, and hope to play an important and positive role in our consumers lives.

Our Strategy

We have implemented a business strategy that emphasizes the following elements:

Extend our knowledge about distressed consumers. We believe our investments in data, analytic tools, and expertise related to both the general and distressed consumer provide us with a competitive advantage. In addition to rigorous data collection practices that take advantage of our unique relationship with distressed consumers, our consumer intelligence program focuses on segmentation, marketing communications, and original research conducted in partnership with experts from both industry and academia. We believe this work will continue to bolster our operational success while fueling our efforts to understand the actions and motivations of our consumer base.

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Realize the full strength of our operations in India. We believe that our operations in India will be critical for both our future collections strategy as well as our future growth. Our call center has expanded considerably over the past few years, and we anticipate that this growth will continue. Our attrition rate for experienced account managers in India is approximately 40% per year in an industry where 100% attrition is not uncommon. Moreover, we have expanded our talented work force in India beyond call center operations and are now developing software, managing portions of our IT infrastructure, handling complex analytics, supporting our bankruptcy servicing teams, and processing a large portion of our back-office needs in India. As portfolio prices fluctuate and the complexity of our industry continues to increase, we expect that our operations in India will continue to provide a significant competitive advantage.

Safeguard and promote financial health and literacy. We believe that our interests, and those of the large financial institutions from which we purchase portfolios, are closely aligned with the interests of government agencies seeking to protect consumer rights. Accordingly, we expect to continue investing in infrastructure and processes that support consumer advocacy and financial literacy, while promoting an appropriate balance between corporate and consumer responsibility.

Consider growth opportunities in adjacent businesses and new geographies. We may consider acquisitions of complementary companies to expand into new markets, add capacity to our current business lines, or leverage our knowledge of the distressed consumer. We believe that our existing underwriting and collection processes can be extended to a variety of charged-off consumer receivables. These capabilities may allow us to develop and provide complimentary products or services to specified distressed consumer segments.

Acquisition of Receivables

We provide sellers of delinquent receivables liquidity and immediate value through the purchase of charged-off consumer receivables. We believe that we are an appealing partner for these sellers given our financial strength, focus on principled intent, and track record of financial success.

Identify purchase opportunities. We maintain relationships with some of the largest credit grantors and sellers of charged-off consumer receivables in the United States. We identify purchase opportunities and secure, where possible, exclusive negotiation rights. We believe that we are a valued partner for primary issuers and sellers from whom we purchase portfolios, and our ability to secure exclusive negotiation rights is typically a result of our strong relationships and our scale of purchasing. Receivable portfolios are sold either through a general auction where the seller requests bids from market participants or through an exclusive negotiation whereby the seller and buyer negotiate the sale privately. The sale transaction can either be for a one-time spot purchase or for a forward flow contract. A forward flow contract is a commitment to purchase receivables over a duration that is typically three to twelve months with specifically defined volume, frequency and pricing. Typically, these contracts have provisions that allow for early termination or price re-negotiation should the underlying quality of the portfolio deteriorate over time or if any particular month s delivery is materially different than the original portfolio used to price the forward flow contract. We generally attempt to secure forward flow contracts for receivables because a consistent volume of receivables over a set duration can allow us more precision in forecasting and planning our operational needs.

Evaluate purchase opportunities using account level analytics. Once a portfolio of interest is identified, we obtain detailed information regarding the included accounts, including certain information regarding the consumers themselves. We then purchase additional information related to credit, savings or payment behavior for the consumer we are contemplating purchasing. Our internal modeling team then analyzes this information to determine the expected value of each potential new consumer. Our collection expectations are based on these demographic data, account characteristics, and economic variables, which we use to predict a consumer s willingness and ability to repay its debt. The expected value of collections for each account is aggregated to calculate an overall value for the portfolio. Additional adjustments are made to account for qualitative factors that may impact the payment behavior of our consumers (such as prior collection activities, or the underwriting approaches of the seller), and servicing related adjustments to ensure our valuations are aligned with our operations.

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Formal approval process. Once we have determined the value of the portfolio and have completed our qualitative diligence, we present the purchase opportunity to our investment committee, which either sets the maximum purchase price for the portfolio based on corporate Internal Rate of Return (IRR) objectives or declines to bid. Members of the investment committee include our CEO, CFO, and other members of our senior management team and experts as needed.

We believe long-term success is best pursued by combining a diverse sourcing approach with an account-level scoring methodology and a disciplined evaluation process.

Collection Approach

We expand and build upon the insight developed during our purchase process when developing our account collection strategies for portfolios we have acquired. Our proprietary consumer-level collectability analysis is the primary determinant of whether an account is actively serviced post-purchase. Throughout our ownership period, we periodically refine this analysis to help determine the most effective collection strategy to pursue for each account. Generally we pursue collection activities on only a fraction of the accounts we purchase, through one or more of our collection channels. The channel identification process is analogous to a decision tree where we first differentiate those consumers who we believe are unable to pay, from those who we believe are. Consumers who we believe are financially incapable of making any payments, or are facing extenuating circumstances or hardships that would prevent them from making payments are excluded from our collection process. It is our practice to assess each consumer s willingness to pay, through analytics, phone calls and/or letters. Despite our efforts to reach consumers and work out a settlement option, only a small number of consumers who we contact choose to engage with us. Those who do are often offered discounts on their obligations, or are presented with payments plans that are intended to suit their needs. However, the majority of consumers we contact ignore our calls and our letters and we must then make the decision about whether to pursue collections through legal means. During 2010, we called approximately 8.6 million unique consumers, of which 1.8 million, or 21%, made contact with us. Similarly, during the same time period, we mailed 8.7 million consumers, of which 3% engaged with us. Throughout our ownership period, we periodically refine our collection approach to determine the most effective collection strategy to pursue for each account. These strategies consist of:

- Inactive. We strive to use our financial resources judiciously and efficiently by not deploying resources on accounts where the prospects of collection are remote. For example, for accounts where we believe that the consumer is currently unemployed, overburdened by debt, incarcerated, or deceased, no collection method of any sort is assigned.

- Direct Mail. We develop innovative, low cost mail campaigns offering consumers appropriate discounts to encourage settlement of their accounts.

- Call Centers. We maintain domestic collection call centers in San Diego, California, Phoenix, Arizona and St. Cloud, Minnesota and an international call center in Gurgaon, India. Each call center consists of multiple collection departments. Account managers supervised by group managers are trained and divided into specialty teams. Account managers use a friendly, but firm, approach to further assess our consumers willingness and capacity to pay. They attempt to work with consumers to evaluate sources and means of repayment to achieve a full or negotiated lump sum settlement or develop payment programs customized to the individual s ability to pay. In cases where a payment plan is developed, account managers encourage consumers to pay through automatic payment arrangements. During our new hire training period, we educate account managers to understand and apply applicable laws and policies that are relevant in the account manager s daily collection activities. Our ongoing training and monitoring efforts help ensure compliance with applicable laws and policies by account managers.

- Skip Tracing. If a consumer s phone number proves inaccurate when an account manager calls an account, or if current contact information for a consumer is not available at the time of account purchase, then the account is automatically routed to our skip tracing process. We currently use a number of different skip tracing companies to provide phone numbers and addresses.

Legal Action. We generally refer accounts for legal action where the consumer has not responded to our direct mail efforts or our calls and it appears the consumer is able, but unwilling, to pay its obligations. When we decide to refer an account for legal action, we retain law firms that specialize in collection matters in the states where we intend to pursue collections. Prior to engaging a collection firm, we evaluate the firm s operations, financial condition, and experience, among other key criteria. We rely on the law firms expertise with respect to applicable debt collection laws to evaluate the accounts we refer to them and to make the decision about whether or not to pursue collection litigation. The law firms we have hired may also attempt to communicate with the consumers in an attempt to collect their debts prior to initiating litigation. We pay the law firms a contingency fee based on amounts they collect on our behalf.

Third Party Collection Agencies. We selectively employ a strategy that uses collection agencies. Collection agencies receive a contingency fee for each dollar collected. Generally, we use these agencies on accounts when we believe they can liquidate better or less expensively than we can or to supplement capacity in our internal call centers. We also use agencies to initially provide us a way to scale quickly when large purchases are made and as a challenger to our internal call center collection teams. Prior to engaging a collection agency, we evaluate, among other things, those aspects of the agency s business that we believe are relevant to its performance and compliance with consumer credit laws and regulations.

Account Balance Transfer. We may transfer to our credit card partners accounts for which this approach offers the highest opportunity for success. The credit card partners may offer the consumer the opportunity to establish new credit and to transfer the balance onto a new credit card. If the account is transferred we receive an agreed-upon payment.

Sale. Beginning in 2010, portfolio sales are not currently part of our strategy. Prior to July 2008, under contractual obligations with Jefferson Capital Systems, LLC, or Jefferson Capital, we sold, on a forward flow basis, all accounts for which the consumer had filed for protection under the United States Bankruptcy Code.

Corporate Compliance and Legal Oversight

Our corporate compliance and legal oversight functions are divided between our legal and financial compliance departments. Our legal department manages regulatory compliance, litigation, corporate transactions, and compliance with our internal ethics policy, while our financial compliance department manages our Sarbanes Oxley 404 compliance, internal audit and Legal Outsourcing audit initiatives.

The legal department is responsible for interpreting and administering our Standards of Business Conduct, which applies to all of our directors, officers, and employees and outlines our commitment to a culture of professionalism and ethical behavior. The Standards promote honest and ethical conduct, including the ethical handling of actual or apparent conflicts of interest between personal and professional relationships, compliance with applicable laws, rules and regulations and full and fair disclosure in reports that we file with, or submit to, the Securities and Exchange Commission and in other public communications made by us. As described in the Standards, we have also established a toll-free Accounting and Fraud Hotline to allow directors, officers, and employees to report any detected or suspected fraud, misappropriations, or other fiscal irregularities, any good faith concern about our accounting and/or auditing practices, or any other violations of the Standards.

Beyond written policies, one of our core internal goals is the adherence to principled intent as it pertains to all consumer interactions. We believe that it is in our shareholders, and our employees best interest to treat all consumers with the highest standards of integrity. Specifically, we have strict policies and a code of ethics which guides all dealings with our consumers. To reinforce existing written policies, we have established a number of quality assurance procedures. Through our Quality Assurance program, our FDCPA training for new account managers and our FDCPA recertification program for continuing account managers, and our Consumer Relations department, we take significant steps to ensure compliance with applicable laws and regulations and seek to promote consumer satisfaction. Our Quality Assurance team aims to enhance the skills of account managers and to drive compliance initiatives through active call monitoring, account manager coaching and mentoring, tracking and distribution of Company-wide best practices. Finally, our Consumer Relations department works directly with consumers to seek to resolve incoming consumer inquiries and to respond to consumer disputes as they may arise.

Information Technology

Technical Infrastructure. Our internal network has been configured to be redundant in all critical functions, at all sites. This backup system has been implemented within the local area network switches, the data center network, and includes our redundant Multiprotocol Label Switching (MPLS) networks. We have the capability to handle high transaction volume in our server network architecture, which can be scaled seamlessly with our future growth plans.

Predictive Dialer Technology. During 2010, we upgraded our predictive dialer technology to accommodate the continued expansion of our call centers. With this upgrade, we expect to have additional call volume capacity and greater efficiency through shorter wait times and an increase in the number of live contacts. We believe this will help maximize account manager productivity and further optimize the yield on our portfolio purchases. We also believe that the use of predictive dialing technology helps us to ensure compliance with certain applicable federal and state laws that restrict the time, place, and manner in which debt collectors can call consumers.

Computer Hardware. We use a robust computer platform to perform our daily operations, including the collection efforts of our global workforce. Because our custom software applications are integrated within our database server environment, we are able to process transaction loads with speed and efficiency. The computer platform offers us reliability and expansion opportunities. Furthermore, this hardware incorporates state of the art data security protection. We back up our data daily, and store copies at a secured off-site location. We also mirror our production data to a remote location to give us full protection in the event of the loss of our primary data center. To ensure the integrity and reliability of our computer platform we periodically engage outside auditors specializing in information technology to examine both our operating systems and disaster recovery plans.

Process Control. To ensure that our entire infrastructure continues to operate efficiently and securely we have developed a strong process and control environment. These controls govern all areas of the enterprise from physical security and virtual security, change management, data protection and segregation of duties.

Ability to Attract and Retain Employees

Of crucial importance to our success is the recruitment and retention of our key employees, account managers, and executive management team. In addition to offering attractive compensation structures for account managers, we may offer employee programs that promote personal and professional goals such as leadership and skills training, tuition assistance in support of continued education, and wellness initiatives that earned us distinction as one of San Diego s Healthiest Employers in 2010. We believe that these tangible benefits, combined with intangible differentiators, such as a diverse employee base and the prospect of living and working in an extremely temperate climate where our Corporate Headquarters is located, all contribute to a sustainable competitive advantage with respect to recruitment and retention.

Competition

The consumer credit recovery industry is highly competitive and fragmented. We compete with a wide range of collection companies, financial services companies, and a number of well-funded entrants with limited experience in our industry. We also compete with traditional contingency collection agencies and in-house recovery departments. Competitive pressures affect the availability and pricing of receivable portfolios, as well as the availability and cost of qualified recovery personnel. In addition, some of our competitors may have signed forward flow contracts under which originating institutions have agreed to transfer charged-off receivables to them in the future, which could restrict those originating institutions from selling receivables to us. We believe some of our major competitors, which include companies that focus primarily on the purchase of charged-off receivable portfolios, have continued to diversify into third-party agency collections and into offering credit card and other financial services as part of their recovery strategy.

When purchasing receivables, we compete primarily on the basis of the price paid for receivable portfolios, the ease of negotiating and closing the prospective portfolio purchases with us, including our ability to obtain funding and our reputation with respect to the quality of services that we provide. We believe that our ability to compete effectively in this market is also dependent upon, among other things, our relationships with originators and sellers of charged-off consumer receivables, and our ability to provide quality collection strategies in compliance with applicable collections laws.

Government Regulation

In a number of states we must maintain licenses to perform debt recovery services and must satisfy related bonding requirements. It is our policy to comply with all material licensing and bonding requirements. Our failure to comply with existing licensing requirements, changing interpretations of existing requirements, or adoption of new licensing requirements, could restrict our ability to collect in states, subject us to increased regulation, increase our costs, or adversely affect our ability to collect our receivables.

Federal and state statutes establish specific guidelines and procedures which debt collectors must follow when collecting consumer receivables. The Fair Debt Collection Practices Act (the FDCPA) and comparable state statutes establish specific guidelines and procedures which debt collectors must follow when communicating with consumers, including the time, place and manner of the communications. It is our policy to comply with the provisions of the FDCPA and comparable state statutes in all of our recovery activities. Our failure to comply with these laws could have a material adverse effect on us if they apply to some or all of our recovery activities. Alongside the FDCPA, the federal laws that apply to our business (in addition to the regulations that relate to these laws) include the following:

- Truth-In-Lending Act
- Fair Credit Billing Act
- Equal Credit Opportunity Act
- Fair Credit Reporting Act
- Electronic Funds Transfer Act
- U.S. Bankruptcy Code
- Credit CARD Act of 2009
- Gramm-Leach-Bliley Act
- Soldiers and Sailors Act
- Health Insurance Portability and Accountability Act
- Dodd-Frank Wall Street Reform and Consumer Protection Act

State laws, among other things, may also limit the interest rate and the fees that a credit originator may impose on our consumers, and also limit the time in which we may file legal actions to enforce consumer accounts.

The relationship between a consumer and a credit card issuer is extensively regulated by federal and state consumer protection and related laws and regulations. While we do not issue credit cards, these laws affect some of our operations because the majority of our receivables originate through credit card transactions. The laws and regulations applicable to credit card issuers, among other things, impose disclosure requirements when a credit card account is advertised, when it is applied for and when it is opened, at the end of monthly billing cycles and at year-end. Federal law requires, among other things, that credit card issuers disclose to consumers the interest rates, fees, grace periods and balance calculation methods associated with their credit card accounts. Some laws prohibit discriminatory practices in connection with the extension of credit. If the originating institution fails to comply with applicable statutes, rules, and regulations, it could create claims and rights for the consumers that

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would reduce or eliminate their obligations under their receivables. When we acquire receivables, we generally require the originating institution to contractually indemnify us against losses caused by its failure to comply with applicable statutes, rules and regulations relating to the receivables before they are sold to us.

Federal statutes further provide that, in some cases, consumers cannot be held liable for, or their liability is limited with respect to, charges to their credit card accounts that resulted from unauthorized use of their credit cards. These laws, among others, may give consumers a legal cause of action against us, or may limit our ability to recover amounts owing with respect to the receivables, whether or not we committed any wrongful act or omission in connection with the account.

State and federal laws concerning identity theft, privacy, data security, the use of automated dialing equipment and other laws related to consumers and consumer protection, as well as laws applicable to specific types of debt, impose requirements or restrictions on collection methods or our ability to enforce and recover certain of our receivables.

The laws described above, among others, as well as any new or changed laws, rules or regulations, may adversely affect our ability to recover amounts owing with respect to our receivables.

Employees

We are a Delaware corporation incorporated in 1999. As of December 31, 2010, we had approximately 1,900 employees. None of our employees is represented by a labor union. We believe that our relations with our employees are good.

Item 1A Risk Factors

This section highlights some specific risks affecting our business, operating results and financial condition. The list of risks is not intended to be exhaustive and the order in which the risks appear is not intended as an indication of their relative weight or importance.

Risk Factors

We are exposed to risks associated with worldwide financial markets and the global economy.

As a result of the global economic downturn, individual consumers are experiencing high unemployment, a lack of credit availability, and depressed real estate values. Continued financial pressure on the consumer on these fronts could reduce our ability to collect on our purchased consumer receivable portfolios and would adversely affect their value. Further, increased financial pressure on the distressed consumer may result in additional regulatory restrictions on our operations and increased litigation filed against us. We are unable to predict the likely duration or severity of the current disruption in financial markets and adverse economic conditions and the effects they may have on our business, financial condition and results of operations.

Our quarterly operating results may fluctuate significantly.

Our quarterly operating results will likely vary in the future due to a variety of factors that could affect our revenues and operating expenses in any particular quarter. We expect that our operating expenses as a percentage of collections will fluctuate in the future as we expand into new markets, increase our new business development efforts, hire additional personnel and incur increased insurance and regulatory compliance costs. In addition, our operating results have fluctuated and may continue to fluctuate as the result of the factors described below and elsewhere in this Annual Report on Form 10-K:

- the timing and amount of collections on our receivable portfolios, including the effects of seasonality and economic recession;

- any charge to earnings resulting from an allowance against the carrying value of our receivable portfolios;

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- increases in operating expenses associated with the growth or change of our operations;
- the cost of credit to finance our purchases of receivable portfolios; and
- the timing and terms of our purchases of receivable portfolios.

Due to fluctuating prices for consumer receivable portfolios, there has been considerable variation in our purchasing volume from quarter to quarter and we expect that to continue. The volume of our portfolio purchases will be limited when prices are high, and may or may not increase when portfolio pricing is more favorable to us. We believe our ability to collect on consumer receivable portfolios may be negatively impacted because of current economic conditions, and this may require us to increase our projected return hurdles in calculating prices we are willing to pay for individual portfolios. An increase in portfolio return hurdles may decrease the volume of portfolios we are successful in purchasing. Because we recognize revenue on the basis of projected collections on purchased portfolios, we may experience variations in quarterly revenue and earnings due to the timing of portfolio purchases.

We may not be able to purchase receivables at sufficiently favorable prices or terms, or at all.

Our ability to continue to operate profitably depends upon the continued availability of receivable portfolios that meet our purchasing standards and are cost-effective based upon projected collections exceeding our costs. Our profitability also depends on our actual collections on accounts meeting or exceeding our projected collections. There is no assurance as to how long portfolios will be available for purchase on terms acceptable to us, or at all.

The availability of consumer receivable portfolios at favorable prices and on favorable terms depends on a number of factors, including:

- continued high levels of default in consumer debt;
- continued sale of receivable portfolios by originating institutions at prevailing price levels;
- our ability to develop and maintain long-term relationships with key major credit originators;
- our ability to obtain adequate data from credit originators or portfolio resellers to appropriately evaluate the collectability of, and estimate the value of, portfolios;
- changes in laws and regulations governing consumer lending, bankruptcy and collections; and
- potential availability of government funding to competing purchasers for the acquisition of account portfolios under various programs intended to serve as an economic stimulus.

In addition, because of the length of time involved in collecting charged-off consumer receivables on acquired portfolios and the volatility in the timing of our collections, we may not be able to identify trends and make changes in our purchasing strategies in a timely manner. Ultimately, if we are unable to continually purchase and collect on a sufficient volume of receivables to generate cash collections that exceed our costs, our business will be materially and adversely affected.

We may experience losses on portfolios consisting of new types of receivables.

We continually look for opportunities to expand the classes of assets that make up the portfolios we acquire. Therefore, we may acquire portfolios consisting of assets with which we have little or no collection experience. Our lack of experience with new types of receivables may cause us to pay too much for these receivable portfolios, which may substantially hinder our ability to generate profits from such portfolios.

Further, our existing methods of collections may prove ineffective for such new receivables, and we may not be able to collect on these portfolios. Our inexperience may have a material and adverse affect on our results of operations.

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We may purchase receivable portfolios that contain unprofitable accounts and we may not be able to collect sufficient amounts to recover our costs and to fund our operations.

We acquire and service receivables that the obligors have failed to pay and the sellers have deemed uncollectible and written off. The originating institutions generally make numerous attempts to recover on their nonperforming receivables, often using a combination of their in-house collection and legal departments as well as third-party collection agencies. In order to operate profitably over the long term, we must continually purchase and collect on a sufficient volume of receivables to generate revenue that exceeds our costs. These receivables are difficult to collect, and we may not be successful in collecting amounts sufficient to cover the costs associated with purchasing the receivables and funding our operations. If we are not able to collect on these receivables or collect sufficient amounts to cover our costs, this may materially and adversely affect our results of operations.

Sellers may deliver portfolios that contain accounts which do not meet our account collection criteria.

In the normal course of our portfolio acquisitions, some receivables may be included in the portfolios that fail to conform to the terms of the purchase agreements and we may seek to return these receivables to the seller for payment or replacement. However, we cannot guarantee that sellers will be able to meet their obligations to us. Accounts that we are unable to return to sellers may yield no return. If sellers deliver portfolios containing too many accounts that do not conform to the terms of the purchase contracts, we may be unable to collect a sufficient amount and the portfolio purchase could be unprofitable, which would have an adverse effect on our cash flows. If cash flows from operations are less than anticipated, our ability to satisfy our debt obligations and purchase new portfolios and our future growth and profitability may be materially and adversely affected.

Our failure to purchase sufficient quantities of receivable portfolios or collect sufficient amounts on receivables we own may necessitate workforce reductions, which may harm our business.

Because fixed costs, such as certain personnel costs and lease or other facilities costs, constitute a significant portion of our overhead, we may be required to reduce the number of employees in our collection operations if we do not continually augment the receivable portfolios we service with additional receivable portfolios or collect sufficient amounts on receivables we own for the reasons indicated above. Reducing the number of employees can affect our business adversely due to:

- lower employee morale, higher employee attrition rates, fewer experienced employees and higher recruiting and training costs;
- disruptions in our operations and loss of efficiency in collection functions; and
- excess costs associated with unused space in collection facilities.

A significant portion of our portfolio purchases during any period may be concentrated with a small number of sellers.

We expect that a significant percentage of our portfolio purchases for any given fiscal year may be concentrated with a few large sellers, some of which also may involve forward flow arrangements. For example, in 2010, we purchased 67% of our portfolios from our five top sellers. We cannot be certain that any of our significant sellers will continue to sell charged-off receivables to us on terms or in quantities acceptable to us, or that we would be able to replace such purchases with purchases from other sellers.

A significant decrease in the volume of purchases available from any of our principal sellers on terms acceptable to us would force us to seek alternative sources of charged-off receivables. We may be unable to find alternative sources from which to purchase charged-off receivables, and even if we could successfully replace such purchases, the search could take time, the receivables could be of lower quality, cost more, or both, any of which could materially adversely affect our financial performance.

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The statistical models we use to project remaining cash flows from our receivable portfolios may prove to be inaccurate.

We use our internally developed Unified Collection Score, or UCS model, and Behavioral Liquidation Score, or BLS model, to project the remaining cash flows from our receivable portfolios. Our UCS and BLS models consider known data about our consumers accounts, including, among other things, our collection experience and changes in external consumer factors, in addition to all data known when we acquired the accounts. There can be no assurance, however, that we will be able to achieve the collections forecasted by our UCS and BLS models. If we are not able to achieve these levels of forecasted collection, our revenues will be reduced or we may be required to record an allowance charge, which may materially and adversely impact our results of operations.

We may incur allowance charges based on the authoritative guidance for loans and debt securities acquired with deteriorated credit quality.

We account for our portfolio revenue in accordance with the authoritative guidance for loans and debt securities acquired with deteriorated credit quality. The authoritative guidance limits the revenue that may be accrued to the excess of the estimate of expected future cash flows over a portfolio s initial cost of accounts receivable acquired, requires that the excess of the contractual cash flows over expected cash flows not be recognized as an adjustment of revenue, expense, or on the balance sheet, and freezes the IRR originally estimated when the accounts receivable are purchased for subsequent allowance testing. Rather than lower the estimated IRR if the expected future cash flow estimates are decreased, the carrying value of our receivable portfolios would be written down to maintain the then-current IRR. Increases in expected future cash flows would be recognized prospectively through an upward adjustment of the IRR over a portfolio s remaining life. Any increased yield then becomes the new benchmark for allowance testing. Since the authoritative guidance does not permit yields to be lowered, there is an increased probability of our having to incur allowance charges in the future, which would negatively impact our results of operations.

Our business of enforcing the collection of purchased receivables is subject to extensive statutory and regulatory oversight, which has increased and may continue to increase.

Laws and regulations applicable to credit card issuers or other debt originators may preclude us from collecting on receivables we purchase, regardless of any act or omission on our part. For instance, we may be precluded from collecting on receivables where the card issuer or originator failed to comply with applicable federal or state laws in generating or servicing the receivables that we have acquired. Because our receivables generally are originated and serviced nationwide, we cannot be certain that the originating lenders have complied with applicable laws and regulations. While our receivable acquisition contracts typically contain provisions indemnifying us for losses owing to the originating institution s failure to comply with applicable laws and other events, we cannot be certain that any indemnities received from originating institutions will be adequate to protect us from losses on the receivables or liabilities to consumers. Laws relating to debt collections also directly apply to our business. Our failure or the failure of third party agencies and attorneys or the originators of our receivables to comply with existing or new laws, rules or regulations could limit our ability to recover on receivables or cause us to pay damages to the original consumers, which could reduce our revenues and harm our business.

We sometimes purchase accounts in asset classes that are subject to industry-specific restrictions that limit the collection methods that we can use on those accounts. Our inability to collect sufficient amounts from these accounts through available collections methods could materially and adversely affect our results of operations.

In response to the global economic downturn, or otherwise, additional consumer protection or privacy laws, rules and regulations may be enacted that impose additional restrictions on the collection of receivables. Such new laws, rules and regulations may materially adversely affect our ability to collect on our receivables, which could materially and adversely affect our earnings.

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Passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act may increase our operational and compliance costs.

The Dodd-Frank Act contains a variety of provisions designed to regulate financial markets, including credit and derivatives transactions. The Dodd-Frank Act requires various federal agencies to adopt a broad range of new rules and regulations, and to prepare numerous studies and reports for Congress. The federal agencies are given significant discretion in drafting the rules and regulations, and consequently, many of the details and much of the impact of the Dodd-Frank Act may not be known for many months or years.

The Dodd-Frank Act will require publicly traded companies to give stockholders a non-binding vote on executive compensation and so-called golden parachute payments, and authorizes the SEC to promulgate rules that would allow stockholders to nominate their own candidates using a company s proxy materials. It is difficult to predict at this time what specific impact the Dodd-Frank Act and the yet to be written implementing rules and regulations will have. However, if the Dodd-Frank Act and the implementing rules and regulations cause a material increase in our compliance and operating costs or materially inhibit our ability to collect on our receivables, they may have a material adverse impact on our results of operations.

Failure to comply with government regulation could result in the suspension or termination of our ability to conduct business, may require the payment of significant fines and penalties, or require other significant expenditures.

The collections industry is heavily regulated under various federal, state and local laws, rules and regulations. Many states and several cities require that we be licensed as a debt collection company. The Federal Trade Commission, state Attorneys General and other regulatory bodies have the authority to investigate a variety of matters including consumer complaints against debt collection companies and to recommend enforcement actions and seek monetary penalties. If we or our third party collection agencies or law firms fail to comply with applicable laws, rules and regulations, including, but not limited to, identity theft, privacy, data security, the use of automated dialing equipment, laws related to consumer protection, debt collection, and laws applicable to specific types of debt, it could result in the suspension or termination of our ability to conduct collection operations, which would materially adversely affect us. Furthermore, our ability to collect may be impacted by state laws which require that certain types of account documentation be in our possession prior to the institution of any collection activities. In addition, new federal, state or local laws or regulations, or changes in the ways these rules or laws are interpreted or enforced, could limit our activities in the future and/or significantly increase the cost of regulatory compliance.

We are dependent upon third parties to service more than half of our consumer receivable portfolios.

We use outside collection services to collect a substantial portion of our receivables. We are dependent upon the efforts of third-party collection agencies and attorneys to service and collect our consumer receivables. Any failure by our third-party collection agencies and attorneys to perform collection services for us adequately or remit such collections to us could materially reduce our revenue and our profitability. In addition, if one or more of those third-party collection agencies or attorneys were to cease operations abruptly, or to become insolvent, such cessation or insolvency could materially reduce our revenue and profitability. Our revenue and profitability could also be materially adversely affected if we were not able to secure replacement third party collection agencies or attorneys or transfer account information to our new third party collection agencies or attorneys or in-house promptly in the event our agreements with our third-party collection agencies and attorneys are terminated. Our revenue and profitability could also be materially adversely affected if our third-party collection agencies or attorneys fail to perform their obligations adequately, or if our relationships with such third-party collection agencies and attorneys otherwise change adversely.

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Increases in costs associated with our collections through a network of attorneys can materially raise our costs associated with our collection strategies and the individual lawsuits brought against consumers to collect on judgments in our favor.

We contract with a nationwide network of attorneys that specialize in collection matters. In connection with our agreements with our contracted attorneys, we advance certain out-of-pocket court costs, or Deferred Court Costs. Deferred Court Costs represent amounts we believe we will recover from our consumers, in addition to the amounts owed on our consumers accounts that we expect to collect. These court costs may be difficult or impossible to collect, and we may not be successful in collecting amounts sufficient to cover the amounts deferred in our financial statements. If we are not able to recover these court costs, this may materially and adversely affect our results of operations.

Further, we are increasing our collection activity through our legal channel and as a consequence, due to an increase in Deferred Court Costs, and an increase in costs related to counterclaims, our costs in collecting on these accounts may increase, which may have a material, adverse effect on our results of operations.

Our network of third party agencies and attorneys may not utilize amounts collected on our behalf or amounts we advance for court costs in the manner for which they were intended.

Third party collection agencies and attorneys may receive funds owed to us. We advance court costs to third party attorneys. These third parties may fail to remit amounts owed to us on a timely matter or at all. Further, third party attorneys may misuse all or some of the funds we advance for court costs. Our ability to recoup our funds may be diminished if these third parties become insolvent or enter into bankruptcy proceedings.

A significant portion of our collections relies upon our success in individual lawsuits brought against consumers and our ability to collect on judgments in our favor.

We generate a significant portion of our revenue by collecting on judgments that are granted by courts in lawsuits filed against consumers. A decrease in the willingness of courts to grant such judgments, a change in the requirements for filing such cases or obtaining such judgments, or a decrease in our ability to collect on such judgments could have a material and adverse effect on our results of operations. As we increase our use of the legal channel for collections, our short-term margins may decrease as a result of an increase in upfront court costs and costs related to counter claims. We may not be able to collect on certain aged accounts because of applicable statutes of limitations and we may be subject to adverse effects of regulatory changes that we cannot predict. Further, courts in certain jurisdictions require that a copy of the account statements or applications be attached to the pleadings in order to obtain a judgment against the consumers. If we are unable to produce account documents, because the account documents have not been provided by the account s seller or otherwise, these courts will deny our claims.

We are subject to ongoing risks of litigation, including individual and class actions under consumer credit, consumer protection, collections, employment, securities and other laws, and may be subject to awards of substantial damages.

We operate in an extremely litigious climate and currently are, and may in the future be, named as defendants in litigation, including individual and class actions under consumer credit, consumer protection, theft, privacy, data security, the use of automated dialing equipment, debt collections, employment, securities and other laws. In addition, we may become subject to regulatory investigations, inquiries and other actions relating to our activities. The litigation and regulatory inquiries in which we are currently engaged or which we may become subject to, could have a material adverse effect on our financial position or results of operations.

Securities class-action litigation has often been filed against companies after a period of volatility in the market price of their stock. Our industry experiences a high volume of litigation, and legal precedents have not

been clearly established in many areas applicable to our business. Additionally, employment-related litigation is

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increasing throughout the country. Defending a lawsuit, regardless of its merit, could be costly and divert management s attention from the operation of our business. Damage awards or settlements could be significant. All of these factors could have an adverse effect on our business and financial condition.

We may make acquisitions that prove unsuccessful or strain or divert our resources.

From time to time, we consider acquisitions of other companies that could complement our business, including the acquisition of entities in diverse geographic regions and entities offering greater access to businesses and markets that we do not currently serve. For instance, during 2005 we acquired Ascension Capital Group and certain assets of Jefferson Capital. We may not be able to successfully acquire other businesses or, if we do, the acquisition may be unprofitable. If we do acquire one or more businesses, we may not successfully operate the businesses acquired, or may not successfully integrate such businesses with our own, which may result in our inability to maintain our goals, objectives, standards, controls, policies, culture or profitability. In addition, through acquisitions, we may enter markets in which we have limited or no experience. The occurrence of one or more of these events may place additional constraints on our resources such as diverting the attention of our management from other business concerns, which may materially adversely affect our operations and financial condition. Moreover, any acquisition may result in a potentially dilutive issuance of equity securities, incurrence of additional debt and amortization of identifiable intangible assets, all of which could reduce our profitability.

We are dependent on our management team for the adoption and implementation of our strategies and the loss of their services could have a material adverse effect on our business.

Our management team has considerable experience in finance, banking, consumer collections and other industries. We believe that the expertise of our executives obtained by managing businesses across numerous other industries has been critical to the enhancement of our operations. Our management team has created a culture of new ideas and progressive thinking, coupled with increased use of technology and statistical analysis. The loss of the services of one or more of our key executive officers could disrupt our operations and seriously impair our ability to continue to acquire or collect on portfolios of charged-off consumer receivables and to manage and expand our business. Our success depends on the continued service and performance of our management team, and we cannot guarantee that we will be able to retain such individuals.

Further, we are developing a senior management succession plan in order to effectively prepare for changes in our executive officers over time, but there can be no guarantee that the plan will be successful or that we will find appropriate candidates. If we are unable to hire and retain qualified employees, our business and operating results could be adversely affected.

Regulatory, political and economic conditions in India expose us to risk, including loss of business.

A significant element of our business strategy is to continue to develop and expand offshore operations in India. While wage costs in India are significantly lower than in the U.S. and other industrialized countries for comparably skilled workers, wages in India are increasing at a faster rate than in the U.S., and we experience higher employee turnover in our operations in India than is typical in our U.S. locations. The continuation of these trends could result in the loss of the cost savings we sought to achieve by establishing a portion of our collection operations to India. In the past, India has experienced significant inflation and shortages of readily available foreign currency for exchange, and has been subject to civil unrest. We may be adversely affected by changes in inflation, exchange rate fluctuations, interest rates, tax provisions, social stability or other political, economic or diplomatic developments in or affecting India in the future. In addition, the infrastructure of the economy in India is relatively poor. Further, the Indian government is significantly involved in and exerts considerable influence over its economy through its complicated tax code and pervasive bureaucracy. In the recent past, the Indian government has provided significant tax incentives and relaxed certain regulatory restrictions in order to encourage foreign investment in certain sectors of the economy, including the technology industry. Changes in the business or regulatory climate of India could have a material and adverse effect on our business, results of operations and financial condition.

We may not be able to manage our growth effectively, including the expansion of our operations in India.

We have expanded significantly in recent years. However, future growth will place additional demands on our resources, and we cannot be sure that we will be able to manage our growth effectively. Continued growth could place a strain on our management, operations and financial resources. We cannot be certain that our infrastructure, facilities and personnel will be adequate to support our future operations or to effectively adapt to future growth. To support our growth and improve our operations, we continue to make investments in infrastructure, facilities and personnel in our operations in the U.S. and in India; however, we cannot be certain that these additional investments will be successful or that our investments will produce profitable results. If we cannot manage our growth effectively, our results of operations may be materially and adversely affected.

The failure of our technology and telecommunications systems could have an adverse effect on our operations.

Our success depends in large part on sophisticated computer and telecommunications systems. The temporary or permanent loss of our computer and telecommunications equipment and software systems, through casualty, operating malfunction, software virus, or service provider failure, could disrupt our operations. In the normal course of our business, we must record and process significant amounts of data quickly and accurately to properly bid on prospective acquisitions of receivable portfolios and to access, maintain and expand the databases we use for our collection activities. Any simultaneous failure of our information systems and their backup systems would interrupt our business operations.

We may not be able to successfully anticipate, invest in or adopt technological advances within our industry.

Our business relies on computer and telecommunications technologies, and our ability to integrate new technologies into our business is essential to our competitive position and our success. We may not be successful in anticipating, managing, or adopting technological changes in a timely basis. Computer and telecommunications technologies are evolving rapidly and are characterized by short product life cycles.

We are making significant modifications to our information systems to ensure that they continue to meet our current and foreseeable demands and continued expansion, and our future growth may require additional investment in these systems. These system modifications may exceed our cost or time estimates for completion or may be unsuccessful. If we cannot update our information systems effectively, our results of operations may be materially and adversely affected.

We depend on having the capital resources necessary to invest in new technologies to acquire and service receivables. We cannot be certain that adequate capital resources will be available to us.

We may not be able adequately to protect the intellectual property rights upon which we rely.

We rely on proprietary software programs and valuation and collection processes and techniques, and we believe that these assets provide us with a competitive advantage. We consider our proprietary software, processes and techniques to be trade secrets, but they are not protected by patent or registered copyright. We may not be able to protect our technology and data resources adequately, which may materially diminish our competitive advantage.

Our results of operations may be materially adversely affected if bankruptcy filings increase or if bankruptcy or other debt collection laws change.

Our business model may be uniquely vulnerable to an economic recession, which typically results in an increase in the amount of defaulted consumer receivables, thereby contributing to an increase in the amount of personal bankruptcy filings. Under certain bankruptcy filings, a consumer s assets are sold to repay credit originators, with priority given to holders of secured debt. Since the defaulted consumer receivables we typically purchase are generally unsecured, we often would not be able to collect on those receivables. In addition, since we purchase receivables that are seriously delinquent, this is often an indication that many of the consumers from whom we collect would be unable to service their debts going forward and are more likely to file for bankruptcy in an economic recession. We cannot be certain that our collection experience would not decline with an increase in bankruptcy filings. If our actual collection experience with respect to a defaulted consumer receivable portfolio is significantly lower than we projected when we purchased the portfolio, our results of operations could be materially and adversely affected.

In 2005, the Bankruptcy Abuse Prevention and Consumer Protection Act, or the Protection Act, was enacted which made significant changes in the treatment of consumer filers for bankruptcy protection. Since the Protection Act was enacted, the number of bankruptcy filings has decreased, and the volume of business at Ascension has decreased as a result. We cannot determine the impact of the Protection Act on the number of bankruptcy filings, on a prospective basis, and its impact on the collectability of consumer debt.

Item 1B Unresolved Staff Comments

None.

Item 2 Properties

Our corporate headquarters and primary operations facility are located in approximately 57,000 square feet of leased space in San Diego, California.

We lease a facility for our call center located in Phoenix, Arizona with approximately 33,000 square feet of space and a facility for our call center located in St. Cloud, Minnesota with approximately 46,000 square feet of space.

Our leased Ascension facility is located in Arlington, Texas and is approximately 28,600 square feet. This facility serves as our bankruptcy servicing center.

We also lease a facility in Gurgaon, India. The facility in India has approximately 107,500 square feet of space and can accommodate approximately 1,600 employees. Our facility in India serves as a call center, bankruptcy servicing center and administrative offices.

We believe that our current leased facilities are generally well maintained and in good operating condition. We believe that these facilities are suitable and sufficient for our operational needs. Our policy is to improve, replace and supplement the facilities as considered appropriate to meet the needs of the individual operations. In this regard, we plan to move certain of our operations to an additional leased facility in San Diego during the coming year to accommodate our anticipated operational needs.

Item 3 Legal Proceedings

On October 18, 2004, Timothy W. Moser, one of our former officers, filed an action in the United States District Court for the Southern District of California against us, and certain individuals, including several of our officers and directors. On February 14, 2005, we were served with an amended complaint in this action alleging defamation, intentional interference with contractual relations, breach of contract, breach of the covenant of good faith and fair dealing, intentional and negligent infliction of emotional distress and civil conspiracy arising out of certain statements in our Registration Statement on Form S-1, originally filed in September 2003, and alleged to be included in our Registration Statement on Form S-3, originally filed in May 2004. The amended complaint sought injunctive relief, economic and punitive damages in an unspecified amount plus an award of profits allegedly earned by the defendants and alleged co-conspirators as a result of the alleged conduct, in addition to attorney s fees and costs. On June 1, 2006, the plaintiff filed a second amended complaint in which he amended his claim for negligent infliction of emotional distress. On January 19, 2010, the District Court issued an order granting defendants summary judgment motions, dismissed all causes of action against all of the defendants and entered judgment in favor of the defendants. On February 12, 2010, Mr. Moser filed a notice of appeal of the judgment. The parties are in the process of briefing their arguments on appeal and no date for oral argument has been set.

On September 7, 2005, Mr. Moser filed a related action in the United States District Court for the Southern District of California against Triarc Companies, Inc. (Triarc), which at the time was a significant stockholder of ours, alleging intentional interference with contractual relations and intentional infliction of emotional distress. The case arose out of the same statements made or alleged to have been made in our Registration Statements referenced above. The amended complaint sought injunctive relief, an order directing Triarc to issue a statement of retraction or correction of the allegedly false statements, economic and punitive damages in an unspecified amount and attorney s fees and costs. Triarc tendered the defense of this action to us, and we accepted the defense and will indemnify Triarc, pursuant to the indemnification provisions of the Registration Rights Agreements dated as of October 31, 2000 and February 21, 2002, and the Underwriting Agreements dated September 25, 2004 and January 20, 2005 to which Triarc is a party. This action was also dismissed by the District Court on January 19, 2010. Mr. Moser s February 12, 2010 appeal also challenges this judgment.

We, along with others in our industry, are routinely subject to legal actions based on the Fair Debt Collection Practices Act, or FDCPA, comparable state statutes and common law causes of action. The violations of law alleged in these actions often include claims that we lack specified licenses to conduct our business, attempt to collect debts on which the statute of limitations has run, and/ or have made inaccurate assertions of fact in support of our collection actions. A number of these cases are styled as class actions and a class has been certified in several of these cases. Many of these cases present novel issues on which there is no clear legal precedent.

In one such action, captioned *Brent v. Midland Credit Management, Inc et. al*, filed on May 19, 2008, in the United States District Court for the Northern District of Ohio Western Division, the plaintiff, Andrea Brent, has filed a class action counter-claim against our subsidiaries Midland Credit Management, Inc. and Midland Funding LLC (the Midland Defendants). The complaint alleges that the Midland Defendants business practices violated consumers rights under the FDCPA and the Ohio Consumer Sales Practices Act. The plaintiff is seeking actual and statutory damages for the class of Ohio residents, plus attorney s fees and costs of class notice and class administration. On August 11, 2009, the court issued an order partially granting plaintiff s motion for summary judgment and entering findings adverse to the Midland Defendants on certain of plaintiff s claims. The Midland Defendants subsequently moved the court to reconsider the order and were partially successful. However, because the court did not completely reverse the August 11 order, certain portions of the order remain subject to reversal only on appeal. On February 22, 2010, the District Court denied Plaintiff s attempts to enlarge the case to include a national class of consumers, and ordered the parties to brief issues relating to whether a statewide class should be certified. On November 4, 2010, the court granted in part, and denied in part, plaintiff s motion for class certification of a statewide class. On February 10, 2011, the parties reached an agreement in principal to settle this lawsuit on a national class basis, subject to entering into a definitive settlement agreement and obtaining court approval after notice to the class. We have vigorously denied the claims asserted against us in this matter, but have agreed to the proposed settlement to avoid the burden and expense of continued litigation. Subject to Court approval, settlement awards to eligible class members, as well as fees and costs, will be paid from a settlement fund of approximately $5.2 million. If the number of class members who make claims exceeds a certain level, the total settlement could increase to an amount not to exceed $5.7 million. Of this, approximately $3.5 million is expected to be paid with insurance proceeds. We have accrued our portion of the settlement, which resulted in a decrease in net income of approximately $1.0 million and a decrease in fully diluted earnings per share of $0.04 for the year ended December 31, 2010.

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We are defending a number of additional class action cases which assert, among other things, affidavit claims similar to those asserted in the *Brent* litigation. Because of the similarities of the claims, the proposed settlement of the *Brent* case is expected to resolve the affidavit claims in these other cases.

On November 2, 2010 and December 17, 2010 two national class actions entitled *Robinson v. Midland Funding LLC* and *Tovar v. Midland Credit Management*, respectively, were filed in the United States District Court for the Southern District of California. The complaints allege that our subsidiaries violated the Telephone Consumer Protection Act (TCPA) by calling consumers cellular phones without their prior express consent. The complaints seek monetary damages under the TCPA, injunctive relief and other relief, including attorney fees. We have filed motions to dismiss or stay these cases. Those motions are currently pending.

There are a number of other lawsuits, claims and counterclaims pending or threatened against us. In general, these lawsuits, claims or counterclaims have arisen in the ordinary course of business and involve claims for damages arising from a variety of alleged misconduct or improper reporting of credit information by us or our employees or agents.

In addition, from time to time, we are subject to various regulatory investigations, inquiries and other actions, relating to our collection activities. These inquiries and other actions include the following:

On January 12, 2011, the Office of the Attorney General of the State of Texas issued a civil investigative demand to us to produce documents in an investigation of our methods of collecting consumer debts in the State of Texas and related topics. We intend to cooperate fully with the Texas Attorney General in response to this subpoena, subject to applicable law.

On January 6, 2010, the Office of the Attorney General of the State of California, the California Attorney General, issued a subpoena to us to answer interrogatories and to produce documents in a proceeding entitled *In the Matter of the Investigation of Encore Capital Group, Inc., Midland Credit Management, Inc. and Affiliated Persons and Entities* concerning our debt collection practices and related topics. We have and intend to continue to cooperate fully with the California Attorney General in response to this subpoena, subject to applicable law.

On December 16, 2009, the Federal Trade Commission, or FTC, issued an order directing us to submit information about our practices in buying and collecting consumer debt, which the FTC intends to use for a study of the debt-buying industry. We are one of nine companies that received such an order from the FTC requesting the production of information for use in the FTC s study of the industry. The nine companies were described by the FTC as the nation s largest consumer debt buyers. The order was publicly announced by the FTC on January 5, 2010. We believe that we have cooperated fully with the FTC in connection with its study, subject to applicable law.

Some of the matters pending against us involve potential compensatory, punitive damage claims, fines or sanctions that, if granted, could require us to pay damages or make other expenditures in amounts that could have a material adverse effect on our financial position or results of operations. In certain of these cases, we may have recourse to insurance or third party contractual indemnities to cover all or portions of our litigation expenses, judgments or settlements. In accordance with authoritative guidance, we have recorded loss contingencies in our financial statements only for matters in which losses are probable and can be reasonably estimated.

Item 4 (Removed and Reserved)

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PART II

Item 5 Market for the Registrant s Common Equity, Related Stockholder Matters and Issuer Purchase of Equity Securities

Our common stock is traded on the NASDAQ Global Select Market under the symbol ECPG.

The high and low sales prices of our common stock, as reported by NASDAQ Global Select Market for each quarter during our two most recent fiscal years, are reported below:

	Market Price	
	High	**Low**
Fiscal Year 2010		
First Quarter	$ 18.66	$ 14.65
Second Quarter	$ 24.09	$ 16.50
Third Quarter	$ 22.92	$ 17.50
Fourth Quarter	$ 23.67	$ 16.70
Fiscal Year 2009		
First Quarter	$ 8.43	$ 2.62
Second Quarter	$ 14.14	$ 4.20
Third Quarter	$ 17.50	$ 10.30
Fourth Quarter	$ 19.89	$ 11.79

The closing price of our common stock on February 1, 2011, was $23.65 per share and there were 17 holders of record, including one representing102 NASD registered broker/dealers.

The following Performance Graph and related information shall not be deemed soliciting material or filed with the SEC, nor shall such information be incorporated by reference into any future filing under the Securities Act of 1933 or Securities Exchange Act of 1934, each as amended, except to the extent that we specifically incorporate it by reference into such filing.

The following graph compares the total cumulative stockholder return on our common stock for the period from December 30, 2005 through December 31, 2010, with the cumulative total return of (a) the NASDAQ Index and (b) Asset Acceptance Capital Corp., Asta Funding, Inc. and Portfolio Recovery Associates, Inc., which we believe are comparable companies. The comparison assumes that $100 was invested on December 30, 2005, in our common stock and in each of the comparison indices.

	12/2005	12/2006	12/2007	12/2008	12/2009	12/2010
Encore Capital Group, Inc.	$ 100.00	$ 72.62	$ 55.79	$ 41.50	$ 100.29	$ 135.16
NASDAQ Composite	$ 100.00	$ 111.74	$ 124.67	$ 73.77	$ 107.12	$ 125.93
Peer Group	$ 100.00	$ 91.86	$ 75.11	$ 41.21	$ 57.61	$ 84.01

Dividend Policy

As a public company, we have never declared or paid dividends on our common stock. However, the declaration, payment and amount of future dividends, if any, is subject to the discretion of our board of directors, which may review our dividend policy from time to time in light of the then existing relevant facts and circumstances. Under the terms of our revolving credit facility, we are permitted to declare and pay dividends in an amount not to exceed, during any fiscal year, 20% of our audited consolidated net income for the then most recently completed fiscal year, so long as no default or unmatured default under the facility has occurred and is continuing or would arise as a result of the dividend payment. We may also be subject to additional dividend restrictions under future financing facilities.

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Item 6 Selected Financial Data

This table presents selected historical financial data of Encore and its consolidated subsidiaries. This information should be carefully considered in conjunction with the consolidated financial statements and notes thereto appearing elsewhere in this report. The selected data in this section are not intended to replace the consolidated financial statements. The selected financial data (except for Selected Operating Data) in the table below, as of December 31, 2008, 2007, and 2006 and for the years ended December 31, 2007 and 2006, were derived from our audited consolidated financial statements not included in this Annual Report on Form 10-K. The selected financial data as of December 31, 2010, and 2009 and for the years ended December 31, 2010, 2009, and 2008, were derived from our audited consolidated financial statements included elsewhere in this Annual Report on Form 10-K. The Selected Operating Data were derived from our books and records *(in thousands, except per share and personnel data):*

	As of and For The Year Ended December 31,				
	2010	**2009**	**2008**	**2007**	**2006**
Revenue					
Revenue from receivable portfolios, net[1]	$ 364,294	$ 299,732	$ 240,802	$ 241,402	$ 239,340
Servicing fees and related revenue[2]	17,014	16,687	15,087	12,609	15,800
Total revenue	381,308	316,419	255,889	254,011	255,140
Operating expenses					
Salaries and employee benefits	65,767	58,025	58,120	64,153	63,962
Stock-based compensation expense	6,010	4,384	3,564	4,287	5,669
Cost of legal collections	121,085	112,570	96,187	78,636	52,079
Other operating expenses	36,387	26,013	23,652	21,533	22,585
Collection agency commissions	20,385	19,278	13,118	12,411	18,030
General and administrative expenses	31,444	26,920	19,445	17,478	17,310
Depreciation and amortization	3,199	2,592	2,814	3,351	3,894
Total operating expenses	284,277	249,782	216,900	201,849	183,529
Income before other (expense) income and income taxes	97,031	66,637	38,989	52,162	71,611
Other (expense) income					
Interest expense	(19,349)	(16,160)	(20,572)	(34,504)	(35,310)
Gain on repurchase of convertible notes, net		3,268	4,771		
Other income (expense)	316	(2)	358	1,071	609
Total other expense	(19,033)	(12,894)	(15,443)	(33,433)	(34,701)
Income before income taxes	77,998	53,743	23,546	18,729	36,910
Provision for income taxes	(28,946)	(20,696)	(9,700)	(6,498)	(15,436)
Net income	$ 49,052	$ 33,047	$ 13,846	$ 12,231	$ 21,474
Earnings per share:					
Basic	$ 2.05	$ 1.42	$ 0.60	$ 0.53	$ 0.94
Diluted	$ 1.95	$ 1.37	$ 0.59	$ 0.52	$ 0.92

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	As of and For The Year Ended December 31, 2010	2009	2008	2007	2006
Weighted-average shares outstanding:					
Basic	23,897	23,215	23,046	22,876	22,754
Diluted	25,091	24,082	23,577	23,386	23,390
Cash flow data:					
Cash flows provided by (used in):					
Operating activities	$ 73,451	$ 76,116	$ 63,071	$ 19,610	$ 38,027
Investing activities	$ (142,807)	$ (79,171)	$ (107,252)	$ (95,059)	$ (37,190)
Financing activities	$ 71,873	$ 1,102	$ 45,846	$ 73,334	$ 2,928
Selected operating data:					
Purchases of receivable portfolios, at cost[3]	$ 361,957	$ 256,632	$ 230,278	$ 208,953	$ 144,287
Gross collections for the period	$ 604,609	$ 487,792	$ 398,633	$ 355,193	$ 337,097
Average active employees for the period[4]	1,563	1,102	913	907	858
Gross collections per average active employee	$ 387	$ 443	$ 436	$ 392	$ 393
Consolidated statements of financial condition data:					
Cash and cash equivalents	$ 10,905	$ 8,388	$ 10,341	$ 8,676	$ 10,791
Investment in receivable portfolios, net	$ 644,753	$ 526,877	$ 461,346	$ 392,209	$ 300,348
Total assets	$ 736,468	$ 595,159	$ 549,079	$ 483,011	$ 394,673
Total debt	$ 385,264	$ 303,075	$ 303,655	$ 256,223	$ 179,010
Total liabilities	$ 433,771	$ 352,068	$ 345,653	$ 295,576	$ 222,803
Total stockholders equity	$ 302,697	$ 243,091	$ 203,426	$ 187,435	$ 171,870

(1) Includes net allowance charges of $22.2 million, $19.3 million, $41.4 million, $11.2 million and $1.4 million for the years ended December 31, 2010, 2009, 2008, 2007 and 2006, respectively.

(2) Includes $16.9 million, $16.7 million, $15.0 million, $12.5 million and $15.7 million in revenue from Ascension for the years ending December 31, 2010, 2009, 2008, 2007 and 2006, respectively.

(3) Purchase price includes a $10.3 million, $5.6 million, $11.7 million and $10.6 million allocation of our forward flow asset for 2009, 2008, 2007 and 2006, respectively. In July 2008, we ceased forward flow purchases from Jefferson Capital due to an alleged breach by Jefferson Capital and its parent, CompuCredit Corporation, of certain agreements. In September 2009, we settled our dispute with Jefferson Capital. As part of the settlement, we purchased a receivable portfolio and applied the remaining forward flow asset to that purchase.

(4) Excludes employees of Ascension and employees in India supporting Ascension, which averaged approximately 191, 125, 116, 133 and 184, for the years ended December 31, 2010, 2009, 2008, 2007 and 2006, respectively.

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Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations

This Annual Report on Form 10-K contains forward-looking statements within the meaning of the securities laws. The words believe, expect, anticipate, estimate, project, intend, plan, will, may and similar expressions often characterize forward-looking statements. These statements may include, but are not limited to, projections of collections, revenues, income or loss, estimates of capital expenditures, plans for future operations, products or services and financing needs or plans, as well as assumptions relating to these matters. Although we believe that the expectations reflected in these forward-looking statements are reasonable, we caution that these expectations or predictions may not prove to be correct or we may not achieve the financial results, savings or other benefits anticipated in the forward-looking statements. These forward-looking statements are necessarily estimates reflecting the best judgment of our senior management and involve a number of risks and uncertainties, some of which may be beyond our control or cannot be predicted or quantified, that could cause actual results to differ materially from those suggested by the forward-looking statements. Many factors, including but not limited to those set forth in this Annual Report on Form 10-K under Part I, Item 1A. Risk Factors, could cause our actual results, performance, achievements or industry results to be very different from the results, performance or achievements expressed or implied by these forward-looking statements. Our business, financial condition or results of operations could also be materially and adversely affected by other factors besides those listed. Forward-looking statements speak only as of the date the statements were made. We do not undertake any obligation to update or revise any forward-looking statements to reflect new information or future events, or for any other reason, even if experience or future events make it clear that any expected results expressed or implied by these forward-looking statements will not be realized. In addition, it is generally our policy not to make any specific projections as to future earnings, and we do not endorse projections regarding future performance that may be made by third parties.

Introduction

We are a leader in consumer debt buying and recovery. We purchase portfolios of defaulted consumer receivables at deep discounts to face value based on robust, account-level valuation methods, and employ a suite of proprietary statistical and behavioral models when building account collection strategies. We use a variety of operational channels to maximize our collections from the portfolios that we purchase, including seeking to partner with individuals as they repay their obligations and work toward financial recovery. In addition, we provide bankruptcy support services to some of the largest companies in the financial services industry through our wholly owned subsidiary Ascension.

While seasonality does not have a material impact on our business, collections are generally strongest in our first calendar quarter, slower in the second and third calendar quarters and slowest in the fourth calendar quarter. Higher relative collections in the first quarter could result in a lower cost-to-collect ratio compared to the fourth quarter, as our fixed costs would be constant and applied against a larger collection base. The seasonal impact on our business may be influenced by our purchasing levels, the types of portfolios we purchase and our operating strategies.

Collection seasonality can also impact our revenue recognition rate. Generally, revenue for each pool group declines steadily over time, whereas collections can fluctuate from quarter to quarter based on seasonality, as described above. In quarters with lower collections (like the 4th calendar quarter), revenue as a percentage of collections can be higher than in quarters with higher collections (like the 1st calendar quarter).

In addition, seasonality could have an impact on the relative level of quarterly earnings. In quarters with stronger collections, total costs are higher, as a result of the additional efforts required to generate those collections. Since revenue for each pool group declines steadily over time, in quarters with stronger collections and higher costs (like the 1st calendar quarter), all else being equal, earnings could be lower than in quarters with slower collections and lower costs (like the 4th calendar quarter).

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Market Overview

While there has been improvement in macroeconomic indicators during 2010, including stronger manufacturing and corporate profit metrics, a broad economic recovery has yet to fully materialize for the U.S. consumer. Minimal job growth, uncertainty over state and federal taxes and limited credit availability continue to challenge U.S. consumers, as demonstrated by weak consumer spending and volatile but rising consumer confidence levels. Within the credit card space, we see mixed signals. Although charge-off rates remain at historic highs, delinquency levels have improved at a rate that may indicate a fundamental improvement in consumer financial strength. However, related measures, like personal bankruptcies and home foreclosures, remain elevated and indicate continued near-term pressure on the average consumer.

Despite this macroeconomic volatility through 2010, most of our internal collection metrics were consistent with, or better than, what we observed in 2008 and 2009. To illustrate, payer rates and average payment size, adjusted for changes in the mix of settlements-in-full versus payment plans, remained constant. However, more of our consumers are opting to settle their debt obligations through payment plans as opposed to one-time settlements. Settlements made through payment plans impact our recoveries in two ways. First, the delay in cash flows from payments received over extended time periods may result in a provision for portfolio allowance. When a long-term payment stream (as compared to a one-time payment of the same amount) is discounted using a pool group s internal rate of return, or IRR, the net present value is lower. In other words, despite the absolute value of total cash received being identical in both scenarios, accounting for the timing of cash flows in a payment plan yields a lower net present value which, in turn, can result in a provision for portfolio allowance. Second, payment plans inherently contain the possibility of consumers failing to complete all scheduled payments, which we term a broken payer.

The rate at which consumers are honoring their obligations and completing their payment plans has increased in 2010 when compared to 2009. We believe this is the result of two factors: our commitment to partner effectively with consumers during their recovery process and the strength of our analytic platform, which allows us to make accurate and timely decisions about how best to maximize our portfolio returns. Nevertheless, payment plans may still produce broken payers that fail to fulfill all scheduled payments. When this happens, we are often successful in getting the consumer back on plan, but this is not always the case and in those instances where we are unable to do so, we experience a shortfall in recoveries as compared to our initial forecasts. Please refer to Management s Discussion and Analysis Revenue below for a more detailed explanation of the provision for portfolio allowances.

Throughout the credit crisis, we strategically invested in receivable portfolio as credit card charge-offs increased to historic levels and we believe that some of our competitors were (i) caught owning receivables with low yields as a result of purchasing certain portfolios at elevated pricing levels between 2005 and 2008 and (ii) faced with constrained access to capital to fund portfolio purchases due to depressed capital markets. These dynamics resulted in a supply-demand gap that dramatically reduced pricing of available portfolios, beginning in early 2009. For example, prices for freshly charged-off assets (i.e., receivables sold within thirty days of charge-off by the credit issuers) declined from a range of 8% 13% in 2008 to a range of 5% 9% in 2009 and early 2010. Similar price reductions were apparent across a broad range of defaulted consumer receivable asset classes (including credit cards and other consumer loans), balance ranges and ages. After such a dramatic decline, pricing has started to increase, but remains favorable when compared to 2005 through 2008 levels. In response to the price declines in 2009 and early 2010, some issuers opted not to sell all of their receivable portfolio and instead, pursued internal liquidation strategies or partnered with third party agencies. We believe that as pricing increases, these issuers will sell a greater percentage of their charged-off portfolios.

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Purchases and Collections

Purchases by Type

The following table summarizes the types of charged-off consumer receivables portfolios we purchased for the periods presented *(in thousands)*:

	Year Ended December 31,		
	2010	2009	2008
Credit card	$ 341,910	$ 256,632	$ 201,315
Consumer bankruptcy receivables[1]	12,205		
Telecom	7,842		28,963
	$ 361,957	$ 256,632	$ 230,278

(1) Represents portfolio receivables subject to Chapter 13 and Chapter 7 bankruptcy proceedings acquired from issuers.

During the year ended December 31, 2010, we invested $362.0 million for portfolios, primarily for charged-off credit card, bankruptcy and telecom portfolios, with face values aggregating $10.9 billion for an average purchase price of 3.3% of face value. This is a $105.4 million increase, or 41.0%, in the amount invested, compared with the $256.6 million invested during the year ended December 31, 2009, to acquire portfolios, primarily consisting of charged-off credit card portfolios, with a face value aggregating $6.5 billion for an average purchase price of 4.0% of face value. Included in our 2010 purchases was a $45.6 million, one-time, large portfolio purchase from one seller in December 2010.

During the year ended December 31, 2009, we invested $256.6 million to acquire portfolios, primarily consisting of charged-off credit card portfolios, with a face value aggregating $6.5 billion for an average purchase price of 4.0% of face value. This is a $26.4 million increase, or 11.4%, in the amount invested, compared with the $230.3 million invested during the year ended December 31, 2008, to acquire portfolios, primarily consisting of charged-off credit card portfolios, with a face value aggregating $6.6 billion for an average purchase price of 3.5% of face value.

Average purchase price, as a percentage of face value, varies from period to period depending on, among other things, the quality of the accounts purchased and the length of time from charge-off to the time we purchase the portfolios.

Collections by Channel

During 2010, 2009 and 2008, we utilized numerous business channels for the collection of charged-off credit card receivables and other charged-off receivables. The following table summarizes gross collections by collection channel *(in thousands)*:

	Year Ended December 31,		
	2010	2009	2008
Collection sites	$ 268,205	$ 185,789	$ 157,077
Legal collections	266,762	232,667	193,201
Collection agencies	68,042	62,653	34,736
Sales		6,677	12,550
Other	1,600	6	1,069
	$ 604,609	$ 487,792	$ 398,633

Gross collections increased $116.8 million, or 23.9%, to $604.6 million during the year ended December 31, 2010, from $487.8 million during the year ended December 31, 2009, primarily due to increased portfolio purchases throughout the year.

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Gross collections increased $89.2 million, or 22.4%, to $487.8 million during the year ended December 31, 2009, from $398.6 million during the year ended December 31, 2008, primarily due to increased portfolio purchases throughout the year.

Results of Operations

Results of operations, in dollars and as a percentage of total revenue, were as follows *(in thousands, except percentages)*:

	Year Ended December 31,					
	2010		2009		2008	
Revenue						
Revenue from receivable portfolios, net	$ 364,294	95.5%	$ 299,732	94.7%	$ 240,802	94.1%
Servicing fees and related revenue	17,014	4.5%	16,687	5.3%	15,087	5.9%
Total revenue	381,308	100.0%	316,419	100.0%	255,889	100.0%
Operating expenses						
Salaries and employee benefits	65,767	17.2%	58,025	18.4%	58,120	22.7%
Stock-based compensation expense	6,010	1.6%	4,384	1.4%	3,564	1.4%
Cost of legal collections	121,085	31.8%	112,570	35.6%	96,187	37.6%
Other operating expenses	36,387	9.5%	26,013	8.2%	23,652	9.2%
Collection agency commissions	20,385	5.4%	19,278	6.1%	13,118	5.1%
General and administrative expenses	31,444	8.2%	26,920	8.5%	19,445	7.6%
Depreciation and amortization	3,199	0.8%	2,592	0.8%	2,814	1.1%
Total operating expenses	284,277	74.5%	249,782	79.0%	216,900	84.7%
Income before other (expense) income and income taxes	97,031	25.5%	66,637	21.0%	38,989	15.3%
Other (expense) income						
Interest expense	(19,349)	(5.1)%	(16,160)	(5.1)%	(20,572)	(8.0)%
Gain on repurchase of convertible notes, net		0.0%	3,268	1.0%	4,771	1.8%
Other income (expense)	316	0.1%	(2)	0.0%	358	0.1%
Total other expense	(19,033)	(5.0)%	(12,894)	(4.1)%	(15,443)	(6.1)%
Income before income taxes	77,998	20.5%	53,743	16.9%	23,546	9.2%
Provision for income taxes	(28,946)	(7.6)%	(20,696)	(6.5)%	(9,700)	(3.8)%
Net income	$ 49,052	12.9%	$ 33,047	10.4%	$ 13,846	5.4%

Comparison of Results of Operations

Year Ended December 31, 2010 Compared to Year Ended December 31, 2009

Revenue

Our revenue consists primarily of portfolio revenue and bankruptcy servicing revenue. Portfolio revenue consists of accretion revenue and zero basis revenue. Accretion revenue represents revenue derived from pools (quarterly groupings of purchased receivable portfolios) with a cost basis that has not been fully amortized. Revenue from pools with a remaining unamortized cost basis is accrued based on each pool s effective interest rate applied to each pool s remaining unamortized cost basis. The cost basis of each pool is increased by revenue earned and decreased by gross collections and portfolio allowances. The effective interest rate is the internal rate of return derived from the timing and amounts of actual cash received and anticipated future cash flow projections for each pool. All collections realized after the net book value of a portfolio has been fully recovered,

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or zero basis portfolios, are recorded as revenue, or zero basis revenue or allowance reversal if applicable. We account for our investment in receivable portfolios utilizing the interest method in accordance with the authoritative guidance for *loans and debt securities acquired with deteriorated credit quality*. Servicing fee revenue is revenue primarily associated with bankruptcy servicing fees earned from our Ascension subsidiary, a provider of bankruptcy services to the finance industry.

The following tables summarize collections, revenue, end of period receivable balance and other related supplemental data, by year of purchase (*in thousands, except percentages*):

	Year Ended December 31, 2010					As of December 31, 2010	
	Collections[1]	Gross Revenue[2]	Revenue Recognition Rate[3]	Net Reversal (Portfolio Allowance)	Revenue % of Total Revenue	Unamortized Balances	Monthly IRR
ZBA	$ 10,590	$ 9,689	91.5%	$ 901	2.5%	$	
2002	417		0.0%	417	0.0%		
2003	3,215	759	23.6%	1,829	0.2%		
2004	7,799	2,822	36.2%	1,553	0.7%	1,166	6.6%
2005	27,034	16,301	60.3%	(2,750)	4.2%	17,315	5.6%
2006	26,185	21,592	82.5%	(9,605)	5.6%	28,890	5.1%
2007	70,569	44,689	63.3%	(4,527)	11.6%	38,302	7.5%
2008	126,496	78,579	62.1%	(10,027)	20.3%	99,802	5.1%
2009	206,360	135,096	65.5%		35.0%	147,830	6.4%
2010	125,729	76,976	61.2%		19.9%	311,448	4.2%
Total	$ 604,394	$ 386,503	63.9%	$ (22,209)	100.0%	$ 644,753	5.1%

	Year Ended December 31, 2009					As of December 31, 2009	
	Collections[1]	Gross Revenue[2]	Revenue Recognition Rate[3]	Net Reversal (Portfolio Allowance)	Revenue % of Total Revenue	Unamortized Balances	Monthly IRR
ZBA	$ 8,927	$ 8,927	100.0%	$	2.8%	$	
2002	2,831	903	31.9%	1,254	0.3%		
2003	8,021	5,932	74.0%	59	1.9%	629	31.4%
2004	11,363	6,922	60.9%	(629)	2.1%	4,600	8.1%
2005	41,948	26,332	62.8%	(2,192)	8.2%	30,804	5.6%
2006	44,554	31,864	71.5%	(4,622)	10.0%	44,030	5.1%
2007	111,116	64,045	57.6%	(6,357)	20.1%	68,739	5.8%
2008	162,846	112,657	69.2%	(6,823)	35.3%	157,807	5.0%
2009	95,852	61,460	64.1%		19.3%	220,268	4.4%
Total	$ 487,458	$ 319,042	65.5%	$ (19,310)	100.0%	$ 526,877	5.0%

(1) Does not include amounts collected on behalf of others.
(2) Gross revenue excludes the effects of net portfolio allowance or net portfolio allowance reversals.
(3) Revenue recognition rate excludes the effects of net portfolio allowance or net portfolio allowance reversals.

Total revenue was $381.3 million for the year ended December 31, 2010, an increase of $64.9 million, or 20.5%, compared to total revenue of $316.4 million for the year ended December 31, 2009. Portfolio revenue was $364.3 million for the year ended December 31, 2010, an increase of $64.6 million, or 21.5%, compared to portfolio revenue of $299.7 million for the year ended December 31, 2009. The increase in portfolio revenue for the year ended December 31, 2010, was primarily the result of additional accretion revenue associated with a higher portfolio balance during the year ended December 31, 2010 compared to the year ended December 31, 2009. During the year ended December 31, 2010, we recorded a net portfolio allowance provision of $22.2

million, compared to a net portfolio allowance provision of $19.3 million in the prior year. The portfolio allowances for the years ended December 31, 2010 and 2009 were largely due to a shortfall in collections in certain pool groups against our forecast. While our total collections exceeded our forecast, there is often variability at the pool group level between our actual collections and our forecasted collections, primarily our 2006 through 2008 vintage portfolios. This is the result of several factors, including pressures on our consumers due to a weakened economy, changes in internal operating strategies, shifts in consumer payment patterns and the inherent challenge of forecasting collections at the pool group level.

Revenue associated with bankruptcy servicing fees was $16.9 million for the year ended December 31, 2010, an increase of $0.2 million, or 1.9%, compared to revenue of $16.7 million for the year ended December 31, 2009.

Operating Expenses

Total operating expenses were $284.3 million for the year ended December 31, 2010, an increase of $34.5 million, or 13.8%, compared to total operating expenses of $249.8 million for the year ended December 31, 2009.

Operating expenses are explained in more detail as follows:

Salaries and employee benefits

Total salaries and employee benefits increased $7.8 million, or 13.3%, to $65.8 million during the year ended December 31, 2010, from $58.0 million during the year ended December 31, 2009. The increase was primarily the result of an additional $9.4 million in payroll related expenses due to increased headcount to support our growth, offset by a $1.6 million decrease in our self-insured health care costs due to our successful wellness programs and to fewer catastrophic claims compared to the prior year.

Stock-based compensation expenses

Stock-based compensation increased $1.6 million, or 37.1%, to $6.0 million during the year ended December 31, 2010, from $4.4 million during the year ended December 31, 2009. This increase was primarily attributable to awards granted to our senior management team in the year ended December 31, 2010 and the higher fair value of equity awards granted in recent periods due to an increase in our stock price.

Cost of legal collections

The cost of legal collections increased $8.5 million, or 7.6%, to $121.1 million during the year ended December 31, 2010, compared to $112.6 million during the year ended December 31, 2009. These costs represent contingent fees paid to our nationwide network of attorneys and costs of litigation. The increase in the cost of legal collections was primarily the result of an increase in commissions paid on increased collections through our legal channel, partially offset by a decrease in court cost expense. For the year ended December 31, 2010, we paid commissions of $76.2 million, or 28.6%, on legal collections of $266.8 million, compared to commissions of $66.5 million, or 28.6%, on legal collections of $232.7 million for the year ended December 31, 2009. Court cost expense decreased to $42.5 million for the year ended December 31, 2010, compared to $43.6 million for the year ended December 31, 2009. This decrease was due to the effect of our change in accounting estimate of Deferred Court Costs effective October 1, 2010, as discussed in more detail in Change in Accounting Estimate under Critical Accounting Policies, which reduced our court cost expense by $2.8 million. This decrease was offset by additional expense related to the increase of $10.7 million in court costs advanced in the year ended December 31, 2010, compared to the year ended December 31, 2009. Accordingly, court cost expense decreased to 15.9% as a percent of legal collections for the year ended December 31, 2010, compared to 18.7% of legal collections for the year ended December 31, 2009. As a result, the cost of legal collections, as a percent of gross collections through this channel, decreased to 45.4% for the year ended

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December 31, 2010 from 48.4% for the year ended December 31, 2009. See Note 5 Deferred Court Costs in our consolidated financial statements for further information on the effect of the change in accounting estimate related to Deferred Court Costs.

The following table summarizes our legal collection channel performance and related direct costs *(in thousands, except percentages)*:

	Year Ended December 31,			
	2010		2009	
Collections	$ 266,762	100.0%	$ 232,667	100.0%
Court costs advanced	$ 74,758	28.0%	$ 64,047	27.5%
Court costs deferred	(32,247)	(12.1)%	(22,169)	(9.5)%
Deferred court costs reversal(1)		0.0%	1,714	0.7%
Court cost expense(2)	42,511	15.9%	43,592	18.7%
Other(3)	2,403	0.9%	2,444	1.1%
Commissions	76,171	28.6%	66,534	28.6%
Total Costs	$ 121,085	45.4%	$ 112,570	48.4%

(1) Primarily related to our settled arbitration with Jefferson Capital in September 2009. As part of the settlement with Jefferson Capital, we returned accounts that were subject to Jefferson Capital s settlement with the FTC. A portion of those accounts were in our legal channel and, when these were returned, resulted in the reversal of court costs previously deferred.

(2) In connection with our agreement with contracted attorneys, we advance certain out-of-pocket court costs. We capitalize these costs in our consolidated financial statements and provide a reserve and corresponding court cost expense for the costs that we believe will be ultimately uncollectible. This amount includes changes in our anticipated recovery rate of court costs expensed.

(3) Other costs consist of costs related to counter claims and legal network subscription fees.

Other operating expenses

Other operating expenses increased $10.4 million, or 39.9%, to $36.4 million during the year ended December 31, 2010, from $26.0 million during the year ended December 31, 2009. The increase was primarily the result of an increase of $2.6 million in direct mail campaign expenses, an increase of $1.7 million in media-related expenses, an increase of $1.9 million in telephone expenses, an increase of $1.1 million in telephone number tracing expenses and a net increase in various other operating expenses of $3.1 million, all to support our growth.

Collection agency commissions

During the year ended December 31, 2010, we incurred $20.4 million in commissions to third party collection agencies, or 30.0% of the related gross collections of $68.0 million, compared to $19.3 million in commissions, or 30.8% of the related gross collections of $62.7 million during the year ended December 31, 2009. The decrease in the net commission rate as a percentage of the related gross collections was primarily due to the mix of accounts placed with the agencies. Commissions, as a percentage of collections through this channel, vary from period to period depending on, among other things, the time from charge-off of the accounts placed with an agency. Generally, freshly charged-off accounts have a lower commission rate than accounts that have been charged off for a longer period of time. During the year ended December 31, 2010, we collected more freshly charged-off accounts with our agencies as compared to the prior year.

General and administrative expenses

General and administrative expenses increased $4.5 million, or 16.8%, to $31.4 million during the year ended December 31, 2010, from $26.9 million during the year ended December 31, 2009. The increase was primarily the result of an increase of $4.1 million in legal settlements, an increase of $0.4 million in consulting

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fees, an increase of $1.4 million in system maintenance costs and a net increase in other general and administrative expenses of $3.8 million. The increase was offset by a decrease of $5.2 million in corporate legal expenses due to incurring significant legal expenses in 2009 in connection with our settled arbitration with Jefferson Capital.

Depreciation and amortization

Depreciation and amortization expense increased $0.6 million, or 23.4%, to $3.2 million during the year ended December 31, 2010, from $2.6 million during the year ended December 31, 2009. The increase was primarily due to increased depreciation expenses resulted from our acquisition of fixed assets in the current and prior years.

Cost per Dollar Collected

The following table summarizes our cost per dollar collected *(in thousands, except percentages)*:

	Year Ended December 31,							
	2010				2009			
	Collections	Cost	Cost Per Channel Dollar Collected	Cost Per Total Dollar Collected	Collections	Cost	Cost Per Channel Dollar Collected	Cost Per Total Dollar Collected
Collection sites	$ 268,205	$ 25,350[1]	9.5%	4.2%	$ 185,789	$ 22,912[1]	12.3%	4.7%
Legal networks	266,762	121,085	45.4%	20.0%	232,667	112,570	48.4%	23.1%
Collection agency outsourcing	68,042	20,385	30.0%	3.4%	62,653	19,278	30.8%	4.0%
Sales and other	1,600				6,683			
Other indirect costs[2]		97,119		16.1%		77,420		15.8%
Total	$ 604,609	$ 263,939[3]		43.7%	$ 487,792	$ 232,180[3]		47.6%

(1) Represents only account manager salaries, variable compensation and employee benefits.

(2) Other indirect costs represent non collection salaries and employee benefits, general and administrative expenses, other operating expenses, and depreciation and amortization.

(3) Represents all operating expenses excluding stock-based compensation expense and bankruptcy servicing operating expenses. We include this information in order to facilitate a comparison of approximate cash costs to cash collections for the debt purchasing business in the periods presented. Refer to the items for reconciliation of operating expenses, excluding stock-based compensation expense and bankruptcy servicing operating expenses to GAAP total operating expenses in the table below.

During the year ended December 31, 2010, cost per dollar collected decreased by 390 basis points to 43.7% of gross collections from 47.6% of gross collections during the year ended December 31, 2009. This decrease was primarily due to several factors, including:

- The cost from our collection sites, which includes account manager salaries, variable compensation and employee benefits, as a percentage of total collections, decreased to 4.2% for the year ended December 31, 2010 from 4.7% for the year ended December 31, 2009 and, as a percentage of our site collections, decreased to 9.5% for the year ended December 31, 2010 from 12.3% for the year ended December 31, 2009. The decrease was primarily due to the growth of our collection workforce in India.

- The cost of legal collections as a percent of total collections decreased to 20.0% for the year ended December 31, 2010 from 23.1% for the year ended December 31, 2009 and, as a percentage of legal collections, decreased to 45.4% in the year ended December 31, 2010 from 48.4% for the year ended December 31, 2009. The decreases were primarily due to the effect of our change in accounting estimate of Deferred Court Costs effective October 1, 2010, as discussed in more detail in Change in Accounting Estimate under Critical Accounting Policies which reduced our court cost expense by $2.8 million. Additionally, as we refine our analytics and increase our ability to model consumer

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behavior, we have been able to be more precise about where to use the legal channel, which has enabled us to reduce our cost expenditure without negatively impacting collections.

The cost of collection agency commissions, as a percentage of total collections, decreased to 3.4% for the year ended December 31, 2010 from 4.0% for the year ended December 30, 2009. The cost in collection agency commissions, as a percentage of channel collections, decreased to 30.0% for the year ended December 31, 2010 from 30.8% for the year ended December 31, 2009. This decrease was the result of a change in the mix of accounts placed into this channel. Freshly charged-off accounts have a lower commission rate than accounts that have been charged-off for a longer period of time. During the year ended December 31, 2010, we collected more freshly charged-off accounts with our agencies as compared to the prior year.

The decrease in cost per dollar collected was partially offset by an increase in other costs not directly attributable to specific channel collections (other indirect costs), as a percentage of total collections, from 15.8% for the year ended December 31, 2009, to 16.1% for the year ended December 31, 2010. These costs include non- collection salaries and employee benefits, general and administrative expenses, other operating expenses and depreciation and amortization. The dollar increase and the increase in cost per dollar collected were due to several factors including increases in corporate settlements and increases in headcount and general and administrative expenses to support our growth.

The following table presents the items for reconciliation of operating expenses, excluding stock-based compensation expense and bankruptcy servicing operating expenses to GAAP total operating expenses *(in thousands*):

	Years Ended December 31,	
	2010	**2009**
GAAP total operating expenses, as reported	$ 284,277	$ 249,782
Stock-based compensation expense	(6,010)	(4,384)
Bankruptcy servicing operating expenses	(14,328)	(13,218)

Expansion in India

Due to the continued strong performance of our team in India and our ability to reduce our overall site cost- to-collect through the expansion of our offshore collection efforts, we have entered into a lease for additional space in India. This space is located adjacent to our current site in Gurgaon, India and will allow us to expand our account manager headcount throughout 2011.

Interest expense

The following table summarizes our interest expense (*in thousands, except percentages*):

	Year Ended December 31,			
	2010	**2009**	**$ Change**	**% Change**
Stated interest on debt obligations	$ 15,667	$ 12,080	$ 3,587	29.7%
Amortization of loan fees and other loan costs	1,669	1,179	490	41.6%
Amortization of debt discount convertible notes	2,013	2,901	(888)	(30.6)%
Total interest expense	$ 19,349	$ 16,160	$ 3,189	19.7%

Stated interest on debt obligations increased $3.6 million during the year ended December 31, 2010, compared to the prior year, primarily due to higher interest rates and increases in amounts borrowed under our revolving credit facility to fund our purchases of receivable portfolios and for general working capital needs.

Other income and expense

During the year ended December 31, 2010, total other income was $0.3 million, compared to a total other expense of less than $0.1 million for the year ended December 31, 2009. The other income of $0.3 million during

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the year ended December 31, 2010 was primarily attributable to a $0.3 million gain recognized in connection with the early termination of a contract.

Provision for income taxes

During the year ended December 31, 2010, we recorded an income tax provision of $28.9 million, reflecting an effective rate of 37.1% of pretax income. The effective tax rate for the year ended December 31, 2010 primarily consisted of a provision for federal income taxes of 32.7% (which is net of a benefit for state taxes of 2.3%), a blended provision for state taxes of 6.7%, a 0.6% beneficial adjustment to federal taxes payable as a result of state tax true ups and a benefit for the effect of permanent book versus tax differences of 1.7%.

During the year ended December 31, 2009, we recorded an income tax provision of $20.7 million, reflecting an effective rate of 38.5% of pretax income. The effective tax rate for the year ended December 31, 2009 primarily consisted of a provision for federal income taxes of 32.4% (which is net of a benefit for state taxes of 2.6%), a blended provision for state taxes of 7.3%, a 1.0% beneficial adjustment to federal taxes payable as a result of state tax rate changes and a benefit for the effect of permanent book versus tax differences of 0.2%.

Year Ended December 31, 2009 Compared to Year Ended December 31, 2008

Revenue

The following tables summarize collections, revenue, end of period receivable balance and other related supplemental data, by year of purchase (*in thousands, except percentages*):

	Year Ended December 31, 2009					As of December 31, 2009	
	Collections(1)	Gross Revenue(2)	Revenue Recognition Rate(3)	Net Reversal (Portfolio Allowance)	Revenue % of Total Revenue	Unamortized Balances	Monthly IRR
ZBA	$ 8,927	$ 8,927	100.0%	$	2.8%	$	
2002	2,831	903	31.9%	1,254	0.3%		
2003	8,021	5,932	74.0%	59	1.9%	629	31.4%
2004	11,363	6,922	60.9%	(629)	2.1%	4,600	8.1%
2005	41,948	26,332	62.8%	(2,192)	8.2%	30,804	5.6%
2006	44,554	31,864	71.5%	(4,622)	10.0%	44,030	5.1%
2007	111,116	64,045	57.6%	(6,357)	20.1%	68,739	5.8%
2008	162,846	112,657	69.2%	(6,823)	35.3%	157,807	5.0%
2009	95,852	61,460	64.1%		19.3%	220,268	4.4%
Total	$ 487,458	$ 319,042	65.5%	$ (19,310)	100.0%	$ 526,877	5.0%

	Year Ended December 31, 2008					As of December 31, 2008	
	Collections(1)	Gross Revenue(2)	Revenue Recognition Rate(3)	Net Reversal (Portfolio Allowance)	Revenue % of Total Revenue	Unamortized Balances	Monthly IRR
ZBA	$ 9,606	$ 9,606	100.0%	$	3.4%	$	
2002	5,511	4,015	72.9%	360	1.4%	681	29.1%
2003	13,874	12,129	87.4%	15	4.3%	2,666	30.7%
2004	19,117	15,121	79.1%	(7,037)	5.4%	9,675	8.3%
2005	66,675	46,115	69.2%	(17,892)	16.3%	48,613	5.6%
2006	70,743	47,922	67.7%	(11,442)	17.0%	61,368	5.1%
2007	145,271	92,928	64.0%	(5,404)	32.9%	122,215	5.2%

2008	67,506	54,366	80.5%		19.3%	216,128	4.9%
Total	$ 398,303	$ 282,202	70.9%	$ (41,400)	100.0%	$ 461,346	5.4%

(1) Does not include amounts collected on behalf of others.
(2) Gross revenue excludes the effects of net portfolio allowance or net portfolio allowance reversals.
(3) Revenue recognition rate excludes the effects of net portfolio allowance or net portfolio allowance reversals.

Total revenue was $316.4 million for the year ended December 31, 2009, an increase of $60.5 million, or 23.7%, compared to total revenue of $255.9 million for the year ended December 31, 2008. Portfolio revenue was $299.7 million for the year ended December 31, 2009, an increase of $58.9 million, or 24.5%, compared to portfolio revenue of $240.8 million for the year ended December 31, 2008. The increase in portfolio revenue for the year ended December 31, 2009, was primarily the result of additional accretion revenue associated with a higher portfolio balance during the year ended December 31, 2009 compared to the year ended December 31, 2008. During the year ended December 31, 2009, we recorded a net portfolio allowance provision of $19.3 million, compared to a net portfolio allowance provision of $41.4 million in the prior year. The net provision for portfolio allowances for the year ended December 31, 2009 was largely due to a shortfall in collections in certain pool groups against our forecast. While our total collections exceeded our forecast, there is often variability at the pool group level between our actual collections and our forecasted collections, primarily our 2006 through 2008 vintage portfolios. This is the result of several factors, including pressures on the consumer due to a weak economy, changes in internal operating strategy, shifts in consumer payment patterns and the inherent challenge of forecasting collections at the pool group level. The net portfolio allowance provision of $41.4 million for the year ended December 31, 2008 was primarily due to a shortfall in collections in certain pool groups against our forecast, primarily our 2004 through 2007 vintages. We believe that this was the result of broadening pressure on our consumers due to a weakening economy as well as to particular challenges we experienced in collecting on certain portfolios.

Revenue associated with bankruptcy servicing fees was $16.7 million for the year ended December 31, 2009, an increase of $1.6 million, or 10.6%, compared to revenue of $15.1 million for the year ended December 31, 2008. The increase in Ascension revenue was due to a higher volume of bankruptcy placements in 2009.

Operating Expenses

Total operating expenses were $249.8 million for the year ended December 31, 2009, an increase of $32.9 million, or 15.1%, compared to total operating expenses of $216.9 million for the year ended December 31, 2008.

Operating expenses are explained in more detail as follows:

Salaries and employee benefits

Total salaries and employee benefits decreased $0.1 million, or less than one percent, to $58.0 million during the year ended December 31, 2009, from $58.1 million during the year ended December 31, 2008. The slight decrease was primarily the result of a decrease of $0.4 million related to deferred compensation expense which was fully amortized in 2008, offset by an increase of $0.4 million in health benefit related expenses. Additionally, total salaries and benefits declined slightly while company headcount increased. This decline is the result of a shift in our collection workforce from the United States to India and a change in our compensation plan structure in our domestic sites.

Stock-based compensation expenses

Stock-based compensation increased $0.8 million, or 23.0%, to $4.4 million during the year ended December 31, 2009, from $3.6 million during the year ended December 31, 2008. This increase was a result of equity awards granted during the year ended December 31, 2009.

Cost of legal collections

The cost of legal collections increased $16.4 million, or 17.0%, to $112.6 million during the year ended December 31, 2009, compared to $96.2 million during the year ended December 31, 2008. These costs represent contingent fees paid to our nationwide network of attorneys and costs of litigation. The increase in the cost of legal collections was primarily the result of an increase in commissions paid on increased collections through our legal channel and an increase in court cost expense. For the year ended December 31, 2009, we paid commissions of $66.5 million, or 28.6%, on legal collections of $232.7 million, compared to commissions of $55.5 million, or 28.7%, on legal collections of $193.2 million for the year ended December 31, 2008. Court costs advanced for the year ended December 31, 2009 amounted to $64.0 million, compared to $63.8 million for the year ended December 31, 2008. Court costs expensed increased to $43.6 million, but decreased to 18.7% as a percent of collections, for the year ended December 31, 2009, compared to $38.5 million, or 19.9% of collections, for the year ended December 31, 2008, due to a decrease in our court cost recovery rate. As a result, the cost of legal collections, as a percent of gross collections through this channel, decreased to 48.4% for the year ended December 31, 2009 from 49.8% for the year ended December 31, 2008.

The following table summarizes our legal collection channel performance and related direct costs *(in thousands, except percentages)*:

	Year Ended December 31,			
	2009		2008	
Collections	$ 232,667	100.0%	$ 193,201	100.0%
Court costs advanced	$ 64,047	27.5%	$ 63,846	33.0%
Court costs deferred	(22,169)	(9.5)%	(25,354)	(13.1)%
Deferred court costs reversal[(1)]	1,714	0.7%		0.0%
Court cost expense[(2)]	43,592	18.7%	38,492	19.9%
Other[(3)]	2,444	1.1%	2,210	1.2%
Commissions	66,534	28.6%	55,485	28.7%
Total Costs	$ 112,570	48.4%	$ 96,187	49.8%

(1) Primarily related to our arbitration settlement with Jefferson Capital in September 2009. As part of the settlement with Jefferson Capital, we returned accounts that were subject to Jefferson Capital s settlement with the FTC. A portion of those accounts were in our legal channel and, when these were returned, resulted in the reversal of court costs previously deferred.

(2) In connection with our agreement with contracted attorneys, we advance certain out-of-pocket court costs. We capitalize these costs in our consolidated financial statements and provide a reserve and corresponding court cost expense for the costs that we believe will be ultimately uncollectible. This amount includes changes in our anticipated recovery rate of court costs expensed.

(3) Other costs consist of costs related to counter claims and legal network subscription fees.

Other operating expenses

Other operating expenses increased $2.3 million, or 10.0%, to $26.0 million during the year ended December 31, 2009, from $23.7 million during the year ended December 31, 2008. The increase was primarily the result of an increase of $0.7 million in telephone expenses, an increase of $0.5 million in telephone number tracing expenses, an increase of $0.5 million in direct mail campaign expenses, an increase of $0.5 million in media-related expenses and a net increase in various other operating expenses of $0.2 million.

Collection agency commissions

During the year ended December 31, 2009, we incurred $19.3 million in commissions to third party collection agencies, or 30.8% of the related gross collections of $62.7 million, compared to $13.1 million in commissions, or 37.8% of the related gross collections of $34.8 million during the year ended December 31, 2008. The increase in commissions was due to the increase in collections through this channel, offset by a lower

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net commission rate. The decrease in the net commission rate as a percentage of the related gross collections was primarily due to the mix of accounts placed with the agencies. Commissions, as a percentage of collections through this channel, vary from period to period depending on, among other things, the time from charge-off of the accounts placed with an agency. Generally, freshly charged-off accounts have a lower commission rate than accounts that have been charged off for a longer period of time. During the year ended December 31, 2009, our agencies collected more from freshly charged-off accounts as compared to the prior year.

General and administrative expenses

General and administrative expenses increased $7.5 million, or 38.4%, to $26.9 million during the year ended December 31, 2009, from $19.4 million during the year ended December 31, 2008. The increase was primarily the result of an increase of $5.3 million in corporate legal expenses related primarily to our settled Jefferson Capital arbitration and other ongoing litigation, an increase of $1.2 million in corporate settlements, an increase of $0.9 million in building rent related to our expansion in India and a net increase in other general and administrative expenses of $0.1 million.

Depreciation and amortization

Depreciation and amortization expense decreased $0.2 million, or 7.9%, to $2.6 million during the year ended December 31, 2009, from $2.8 million during the year ended December 31, 2008. Depreciation expense was $2.0 million for the years ended December 31, 2009 and December 31, 2008. Amortization expense, relating to intangible assets acquired in conjunction with the acquisition of Ascension in 2005, was $0.6 million for the year ended December 31, 2009, compared to $0.8 million for the year ended December 31, 2008.

Cost per Dollar Collected

The following table summarizes our cost per dollar collected *(in thousands, except percentages*):

	Year Ended December 31,							
	2009				2008			
	Collections	Cost	Cost Per Channel Dollar Collected	Cost Per Total Dollar Collected	Collections	Cost	Cost Per Channel Dollar Collected	Cost Per Total Dollar Collected
Collection sites	$ 185,789	$ 22,912[1]	12.3%	4.7%	$ 157,077	$ 25,267[1]	16.1%	6.3%
Legal networks	232,667	112,570	48.4%	23.1%	193,201	96,187	49.8%	24.1%
Collection agency outsourcing	62,653	19,278	30.8%	4.0%	34,736	13,118	37.8%	3.3%
Sales and other	6,683				13,619			
Other indirect costs[2]		77,420		15.8%		65,395		16.5%
Total	$ 487,792	$ 232,180[3]		47.6%	$ 398,633	$ 199,967[3]		50.2%

(1) Represents only account manager salaries, variable compensation and employee benefits.

(2) Other indirect costs represent non collection salaries and employee benefits, general and administrative expenses, other operating expenses, and depreciation and amortization.

(3) Represents all operating expenses excluding stock-based compensation expense and bankruptcy servicing operating expenses. We include this information in order to facilitate a comparison of approximate cash costs to cash collections for the debt purchasing business in the periods presented. Refer to the items for reconciliation of operating expenses, excluding stock-based compensation expense and bankruptcy servicing operating expenses to GAAP total operating expenses in the table below.

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During the year ended December 31, 2009, cost per dollar collected decreased by 260 basis points to 47.6% of gross collections from 50.2% of gross collections during the year ended December 31, 2008. This decrease was primarily due to several factors, including:

- The cost of legal collections increased in total dollars but decreased as a percent of total collections to 23.1% from 24.1% and, as a percentage of legal collections, decreased to 48.4% from 49.8%. The dollar increase is primarily due to an increase in collections through this channel. The decrease in the percentage is primarily due to commissions and court cost expense growing at a rate slower than total collections.

- Account manager salaries, variable compensation and employee benefits, as a percentage of total collections, decreased to 4.7% from 6.3% and, as a percentage of our site collections, decreased to 12.3% from 16.1%. The decrease is primarily due to a shift in our collection workforce from the United States to India and a change in our compensation plan structure in the United States.

- Other costs not directly attributable to specific channel collections, including non-collection salaries and employee benefits, general and administrative expenses, other operating expenses and depreciation and amortization, decreased as a percentage of total collection to 15.8% from 16.5%. This decrease is primarily due to the increased leverage of spreading our non direct collection costs over a larger pool of collections. The dollar increase is due to several factors including increases in corporate legal expense related primarily to our settled Jefferson Capital arbitration and other ongoing litigation, an increase in corporate settlements and other increases to support our growth.

The decrease in cost per dollar collected was offset by an increase in collection agency commissions, as a percentage of total collections, to 4.0% from 3.3%. The increase in the percentage of commissions to total collections is due to collection agency collections growing at a rate faster than total collections, offset by a decline in the commission rate due to our agencies collecting more from freshly charged-off accounts during the year ended December 31, 2009 than they did during the year ended December 31, 2008. Freshly charged-off accounts have a lower commission rate than accounts that have been charged off for a longer period of time. This resulted in a decline in cost per dollar collected in this channel from 37.8% to 30.8%.

The following table presents the items for reconciliation of operating expenses, excluding stock-based compensation expense and bankruptcy servicing operating expenses to GAAP total operating expenses *(in thousands)*:

	Years Ended December 31,	
	2009	**2008**
GAAP total operating expenses, as reported	$ 249,782	$ 216,900
Stock-based compensation expense	(4,384)	(3,564)
Bankruptcy servicing operating expenses	(13,218)	(13,369)

Interest expense

Interest expense decreased $4.4 million, or 21.4%, to $16.2 million during the year ended December 31, 2009, from an adjusted $20.6 million during the year ended December 31, 2008.

The following table summarizes our interest expense (*in thousands*):

	Year Ended December 31,			
	2009	**2008**	**$ Change**	**% Change**
Stated interest on debt obligations	$ 12,080	$ 14,252	$ (2,172)	(15.2)%
Amortization of loan fees and other loan costs	1,179	1,213	(34)	(2.8)%
Amortization of debt discount convertible notes	2,901	5,107	(2,206)	(43.2)%
Total interest expense	$ 16,160	20,572	$ (4,412)	(21.4)%

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Stated interest on debt obligations decreased $2.2 million during the year ended December 31, 2009, compared to the prior year, primarily due to decreases in our variable interest rate on our revolving credit facility and decreased stated interest expense on our convertible notes due to a reduced principal balance as a result of buy backs, offset by increases in amounts borrowed under our revolving credit facility to fund our purchases of receivable portfolios, to fund our repurchases of a portion of our convertible notes and for general working capital needs.

Gain on repurchase of convertible notes, net

During the year ended December 31, 2009, we repurchased $28.5 million principal amount of our outstanding convertible notes, for a total price of $22.3 million, plus accrued interest. The repurchases left $42.9 million principal amount of our convertible notes outstanding as of December 31, 2009. These repurchases resulted in a pre-tax gain of $3.5 million, which was partially offset by a $0.2 million write-off of the debt issuance costs related to the portions of the convertible notes repurchased. The net gain of $3.3 million was recognized in our consolidated statement of operations for the year ended December 31, 2009.

Other income and expense

During the year ended December 31, 2009, total other expense was less than $0.1 million, compared to $0.4 million for the year ended December 31, 2008. The other income of $0.4 million during the year ended December 31, 2008 was primarily attributable to a $0.3 million gain recognized in connection with the early termination of a contract.

Provision for income taxes

During the year ended December 31, 2009, we recorded an income tax provision of $20.7 million, reflecting an effective rate of 38.5% of pretax income. The effective tax rate for the year ended December 31, 2009 primarily consisted of a provision for federal income taxes of 32.4% (which is net of a benefit for state taxes of 2.6%), a blended provision for state taxes of 7.3%, a 1.0% beneficial adjustment to federal taxes payable as a result of state tax rate changes and a benefit for the effect of permanent book versus tax differences of 0.2%.

During the year ended December 31, 2008, we recorded an income tax provision of $9.7 million, reflecting an effective rate of 41.2% of pretax income. The effective tax rate for the year ended December 31, 2008, primarily consisted of a provision for federal income taxes of 32.3% (which is net of a benefit for state taxes of 2.7%), a blended provision for state taxes of 7.8%, a 1.2% adjustment to federal taxes payable as a result of state tax rate changes and a benefit for the effect of permanent book versus tax differences of 0.1%.

The overall income tax rate for the year ended December 31, 2009, decreased to 38.5% from 41.2% for the year ended December 31, 2008. This decrease was primarily due to a net state effective tax rate decrease in 2009, the release of a tax reserve and a true-up of certain tax amounts.

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Supplemental Performance Data

Cumulative Collections to Purchase Price Multiple

The following table summarizes our purchases and related gross collections by year of purchase (in thousands, except multiples):

Year of		Cumulative Collections through December 31, 2010									
Purchase	Purchase Price[1]	<2004	2004	2005	2006	2007	2008	2009	2010	Total[2]	CCM[3]
<2004	$ 284,159[4]	$ 517,451	$ 192,940	$ 144,775	$ 109,379	$ 50,708	$ 26,777	$ 16,345	$ 11,924	$ 1,070,299	3.8
2004	101,320		39,400	79,845	54,832	34,625	19,116	11,363	8,062	247,243	2.4
2005	192,585			66,491	129,809	109,078	67,346	42,387	27,210	442,321	2.3
2006	141,031				42,354	92,265	70,743	44,553	26,201	276,116	2.0
2007	204,278					68,048	145,272	111,117	70,572	395,009	1.9
2008	227,897						69,049	165,164	127,799	362,012	1.6
2009	253,479							96,529	206,773	303,302	1.2
2010	358,491								125,853	125,853	0.4
Total	$ 1,763,240	$ 517,451	$ 232,340	$ 291,111	$ 336,374	$ 354,724	$ 398,303	$ 487,458	$ 604,394	$ 3,222,155	1.8

(1) Adjusted for put-backs, account recalls, purchase price rescissions, and the impact of an acquisition in 2000. Put-backs represent accounts that are returned to the seller in accordance with the respective purchase agreement (Put-Backs). Recalls represents accounts that are recalled by the seller in accordance with the respective purchase agreement (Recalls).

(2) Cumulative collections from inception through December 31, 2010, excluding collections on behalf of others.

(3) Cumulative Collections Multiple (CCM) through December 31, 2010 collections as a multiple of purchase price.

(4) From inception through December 31, 2003.

Total Estimated Collections to Purchase Price Multiple

The following table summarizes our purchases, resulting historical gross collections, and estimated remaining gross collections, by year of purchase *(in thousands, except multiples)*:

	Purchase Price[1]	Historical Collections[2]	Estimated Remaining Collections	Total Estimated Gross Collections	Total Estimated Gross Collections to Purchase Price
<2004	$ 284,159[3]	$ 1,070,299	$ 1,028	$ 1,071,327	3.8
2004	101,320	247,243	1,679	248,922	2.5
2005	192,585	442,321	26,914	469,235	2.4
2006	141,031	276,116	54,008	330,124	2.3
2007	204,278	395,009	93,862	488,871	2.4
2008	227,897	362,012	204,134	566,146	2.5
2009	253,479	303,302	344,994	648,296	2.6
2010	358,491	125,853	662,193	788,046	2.2
Total	$ 1,763,240	$ 3,222,155	$ 1,388,812	$ 4,610,967	2.6

(1) Adjusted for Put-Backs, Recalls, purchase price rescissions, and the impact of an acquisition in 2000.

(2) Cumulative collections from inception through December 31, 2010, excluding collections on behalf of others.

(3) From inception through December 31, 2003.

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Estimated Remaining Gross Collections by Year of Purchase

The following table summarizes our estimated remaining gross collections by year of purchase *(in thousands)*:

	Estimated Remaining Gross Collections by Year of Purchase							
	2011	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**Total**
<2004[1]	$ 1,028	$	$	$	$	$	$	$ 1,028
2004	1,679							1,679
2005	19,968	6,929	17					26,914
2006	25,415	19,293	9,300					54,008
2007	45,021	27,779	15,735	5,327				93,862
2008	88,831	55,309	34,482	18,901	6,611			204,134
2009	149,054	101,057	49,907	27,099	13,069	4,808		344,994
2010	209,299	199,635	115,828	67,621	39,291	21,796	8,723	662,193
Total	$ 540,295	$ 410,002	$ 225,269	$ 118,948	$ 58,971	$ 26,604	$ 8,723	$ 1,388,812

(1) Estimated remaining collections for Zero Basis Portfolios can extend beyond the 84-month accrual basis collection forecast.

Unamortized Balances of Portfolios

The following table summarizes the remaining unamortized balances of our purchased receivable portfolios by year of purchase *(in thousands, except percentages)*:

	Unamortized Balance as of December 31, 2010	**Purchase Price[1]**	**Unamortized Balance as a Percentage of Purchase Price**	**Unamortized Balance as a Percentage of Total**
2004	$ 1,166	$ 101,320	1.2%	0.2%
2005	17,315	192,585	9.0%	2.7%
2006	28,890	141,031	20.5%	4.5%