

ENCORE CAPITAL GROUP INC

Form 10-Q

July 30, 2009

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2009

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
(State or other jurisdiction of
incorporation or organization)

8875 Aero Drive, Suite 200

San Diego, California
(Address of principal executive offices)

48-1090909
(IRS Employer
Identification No.)

92123
(Zip code)

(877) 445-4581

(Registrant's telephone number, including area code)

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(Not Applicable)

(Former name, former address and former fiscal year, if changed since last report)

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 last 90 days. Yes No

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

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

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at July 21, 2009
Common Stock, \$0.01 par value	23,139,790 shares

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ENCORE CAPITAL GROUP, INC.

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Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Condensed Consolidated Financial Statements (Unaudited)
ENCORE CAPITAL GROUP, INC.****Condensed Consolidated Statements of Financial Condition**

(In Thousands, Except Par Value Amounts)

(Unaudited)

	June 30, 2009	December 31, 2008 Adjusted
Assets		
Cash and cash equivalents	\$ 5,935	\$ 10,341
Accounts receivable, net	3,385	1,757
Investment in receivable portfolios, net	506,708	461,346
Deferred court costs	29,760	28,335
Property and equipment, net	6,750	6,290
Prepaid income tax		7,935
Forward flow asset	10,302	10,302
Other assets	5,073	5,049
Goodwill	15,985	15,985
Identifiable intangible assets, net	1,418	1,739
Total assets	\$ 585,316	\$ 549,079
Liabilities and stockholders equity		
Liabilities:		
Accounts payable and accrued liabilities	\$ 19,410	\$ 18,204
Income tax payable	686	
Deferred tax liabilities, net	15,468	15,108
Deferred revenue and purchased servicing obligation	5,400	5,203
Debt	320,340	303,655
Other liabilities	2,648	3,483
Total liabilities	363,952	345,653
Commitments and contingencies		
Stockholders equity:		
Convertible preferred stock, \$.01 par value, 5,000 shares authorized, no shares issued and outstanding		
Common stock, \$.01 par value, 50,000 shares authorized, 23,138 shares and 23,053 shares issued and outstanding as of June 30, 2009, and December 31, 2008, respectively	231	231
Additional paid-in capital	100,321	98,521
Accumulated earnings	122,433	106,795
Accumulated other comprehensive loss	(1,621)	(2,121)
Total stockholders equity	221,364	203,426
Total liabilities and stockholders equity	\$ 585,316	\$ 549,079

See accompanying notes to unaudited condensed consolidated financial statements

Table of Contents**ENCORE CAPITAL GROUP, INC.****Condensed Consolidated Statements of Income**

(In Thousands, Except Per Share Amounts)

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008 Adjusted	2009	2008 Adjusted
Revenue				
Revenue from receivable portfolios, net	\$ 73,965	\$ 66,275	\$ 146,240	\$ 130,343
Servicing fees and other related revenue	4,070	3,745	8,241	7,231
Total revenue	78,035	70,020	154,481	137,574
Operating expenses				
Salaries and employee benefits (excluding stock-based compensation expense)	14,762	15,689	28,719	30,540
Stock-based compensation expense	994	1,228	2,074	2,322
Cost of legal collections	28,626	23,829	58,573	44,135
Other operating expenses	6,598	5,987	12,578	11,638
Collection agency commissions	4,797	3,781	7,688	7,812
General and administrative expenses	7,097	4,581	12,794	9,041
Depreciation and amortization	620	766	1,243	1,488
Total operating expenses	63,494	55,861	123,669	106,976
Income before other (expense) income and income taxes	14,541	14,159	30,812	30,598
Other (expense) income				
Interest expense	(3,958)	(4,831)	(8,231)	(10,031)
Gain on repurchase of convertible notes, net	215	707	3,268	707
Other income (expense)	9	352	(72)	373
Total other expense	(3,734)	(3,772)	(5,035)	(8,951)
Income before income taxes	10,807	10,387	25,777	21,647
Provision for income taxes	(4,166)	(4,225)	(10,139)	(8,734)
Net income	\$ 6,641	\$ 6,162	\$ 15,638	\$ 12,913
Weighted average shares outstanding:				
Basic	23,168	23,007	23,145	23,000
Diluted	23,971	23,512	23,811	23,468
Earnings per share:				
Basic	\$ 0.29	\$ 0.27	\$ 0.68	\$ 0.56
Diluted	\$ 0.28	\$ 0.26	\$ 0.66	\$ 0.55

See accompanying notes to unaudited condensed consolidated financial statements

Table of Contents**ENCORE CAPITAL GROUP, INC.****Condensed Consolidated Statements of Stockholders Equity**

(Unaudited, In Thousands)

	Common Stock		Additional	Accumulated	Accumulated	Total	Comprehensive
	Shares	Par	Paid-In	Earnings	(Loss)	Equity	Income
			Capital		Income		
Balance at December 31, 2008, Adjusted	23,053	\$ 231	\$ 98,521	\$ 106,795	\$ (2,121)	\$ 203,426	
Net income				15,638		15,638	15,638
Other comprehensive income:							
Unrealized gain on cash flow hedge, net of tax					500	500	500
Issuance of share-based awards	85		(231)			(231)	
Stock-based compensation			2,074			2,074	
Tax provision related to stock option exercises			(43)			(43)	
Balance at June 30, 2009	23,138	\$ 231	\$ 100,321	\$ 122,433	\$ (1,621)	\$ 221,364	\$ 16,138

See accompanying notes to unaudited condensed consolidated financial statements

Table of Contents**ENCORE CAPITAL GROUP, INC.****Condensed Consolidated Statements of Cash Flows**

(Unaudited, In Thousands)

	Six Months Ended June 30,	
	2009	2008 Adjusted
Operating activities:		
Net Income	\$ 15,638	\$ 12,913
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,243	1,488
Amortization of loan costs and debt discount	2,160	3,110
Stock-based compensation expense	2,074	2,322
Gain on repurchase of convertible notes, net	(3,268)	(707)
Deferred income tax expense	360	36
Tax provision from stock-based payment arrangements	43	12
Provision for impairment on receivable portfolios, net	9,991	8,725
Changes in operating assets and liabilities		
Other assets	(2,456)	1,008
Deferred court costs	(1,425)	(4,622)
Prepaid income tax and income tax payable	8,577	8,846
Deferred revenue and purchased service obligation	197	472
Accounts payable, accrued liabilities and other liabilities	611	(217)
Net cash provided by operating activities	33,745	33,386
Investing activities:		
Purchases of receivable portfolios, net of forward flow allocation	(137,946)	(94,833)
Collections applied to investment in receivable portfolios, net	81,163	67,272
Proceeds from put-backs of receivable portfolios	1,430	2,047
Purchases of property and equipment	(1,400)	(2,034)
Net cash used in investing activities	(56,753)	(27,548)
Financing activities:		
Proceeds from revolving credit facility	62,500	15,000
Repayment of revolving credit facility	(21,500)	(17,169)
Repurchase of convertible notes	(22,262)	(3,500)
Proceeds from exercise of stock options	29	8
Tax provision from stock-based payment arrangements	(43)	(12)
Repayment of capital lease obligations	(122)	(145)
Net cash provided by (used in) financing activities	18,602	(5,818)
Net (decrease) increase in cash	(4,406)	20
Cash and cash equivalents, beginning of period	10,341	8,676
Cash and cash equivalents, end of period	\$ 5,935	\$ 8,696
Supplemental disclosures of cash flow information:		
Cash paid for interest	\$ 6,435	\$ 6,792

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Income tax payment (refund)	\$ 1,626	\$ (236)
Supplemental schedule of non-cash investing and financing activities:		
Allocation of forward flow asset to acquired receivable portfolios	\$	\$ 2,926
<i>See accompanying notes to unaudited condensed consolidated financial statements</i>		

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ENCORE CAPITAL GROUP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1: Ownership, Description of Business and Summary of Significant Accounting Policies

Encore Capital Group, Inc. (Encore), through its subsidiaries (collectively, the Company), is a systems-driven purchaser and manager of charged-off consumer receivable portfolios and, through its wholly owned subsidiary Ascension Capital Group, Inc. (Ascension), a provider of bankruptcy services to the finance industry. The Company acquires its receivable portfolios at deep discounts from their face values using its proprietary valuation process that is based on the consumer attributes of the underlying accounts. Based upon the Company s ongoing analysis of these accounts, it employs a dynamic mix of collection strategies to maximize its return on investment. The receivable portfolios the Company purchases consist primarily of unsecured, charged-off domestic consumer credit card, auto deficiency and telecom receivables purchased from national financial institutions, major retail credit corporations, telecom companies and resellers of such portfolios. Acquisitions of receivable portfolios are financed by operations and by borrowings from third parties. See Note 7 for further discussion of the Company s debt.

Financial Statement Preparation

The accompanying interim condensed consolidated financial statements have been prepared by Encore, without audit, in accordance with the instructions to Form 10-Q, and Rule 10-01 of Regulation S-X promulgated by the Securities and Exchange Commission and, therefore, do not include all information and footnotes necessary for a fair presentation of its consolidated financial position, results of operations and cash flows in accordance with accounting principles generally accepted in the United States.

In the opinion of management, the unaudited financial information for the interim periods presented reflects all adjustments, consisting of only normal and recurring adjustments, necessary for a fair presentation of the Company s consolidated results of operations, financial position and cash flows. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements included in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2008. Operating results for interim periods are not necessarily indicative of operating results for an entire fiscal year.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts and the disclosure of contingent amounts in the Company s financial statements and the accompanying notes. Actual results could materially differ from those estimates.

Principles of Consolidation

The Company s condensed consolidated financial statements include the assets, liabilities and operating results of its wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated.

Change in Accounting Principle

Effective January 1, 2009, the Company retrospectively applied Financial Accounting Standard Board (FASB) Staff Position APB 14-1 (FSP APB 14-1) *Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)* to account for its outstanding convertible senior notes. As a result, prior years consolidated financial statements have been retrospectively adjusted. See Note 12 for additional information on the application of this accounting principle.

Reclassification

The prior year s consolidated statement of cash flows has been changed to the indirect method, to conform to the current year s presentation. Additionally, certain reclassifications have been made to the consolidated financial statements to conform to the current year s presentation.

Earnings per Share

Basic earnings per share (EPS) is calculated by dividing net earnings available to common stockholders by the weighted average number of shares of common stock outstanding. Common stock outstanding includes shares of common stock and restricted stock units for which no future

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service is required as a condition to the delivery of the underlying common stock. Diluted EPS includes the determinants of basic EPS and, in addition, reflects the dilutive effect of the common stock deliverable pursuant to stock options and

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to restricted stock units for which future service is required as a condition to the delivery of the underlying common stock. Employee stock options to purchase approximately 1,346,000 shares of common stock during the three and six months ended June 30, 2009, and employee stock options to purchase approximately 1,298,000 shares of common stock during the three and six months ended June 30, 2008, were outstanding but not included in the computation of diluted earnings per share because the effect on diluted earnings per share would be anti-dilutive.

New Accounting Pronouncements

In December 2008, the FASB released FSP FAS 132(R)-1, *Employers' Disclosures about Postretirement Benefit Plan Assets*, which amends Statement of Financial Accounting Standard No. 132R to provide guidance on an employer's disclosures about plan assets of a defined benefit pension or other postretirement plan. This FASB Staff Position is effective for financial statements issued for fiscal years ending after December 15, 2009. The Company expects to adopt this new standard and its required disclosures in its consolidated financial statements for the fiscal year ending December 31, 2009.

In June 2009, the FASB issued FAS No. 166, a revision to FAS No. 140, *Accounting for Transfers of Financial Assets*, and will require more information about transferred financial assets and where companies have continuing exposure to the risks related to transferred financial assets. This standard is effective at the start of a company's first fiscal year beginning after November 15, 2009, or January 1, 2010 for companies reporting earnings on a calendar-year basis. The Company is currently analyzing the impact of this statement, if any, to its consolidated financial statements.

In June 2009, the FASB issued FAS No. 168, *The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting*. This standard represents the last numbered standard issued by FASB under the old (pre-Codification) numbering system, and amends the GAAP hierarchy. On July 1, FASB launched FASB's new Codification (*i.e.* the FASB Accounting Standards Codification). The Codification supersedes existing GAAP for nongovernmental entities. The Company will revise its financial statement disclosure in compliance with the new codification system effective in its third quarter ended September 30, 2009.

Note 2: Fair Value Measurement

On January 1, 2008, the Company adopted Statement of Financial Accounting Standard No. 157, *Fair Value Measurements* (FAS 157), for financial assets and liabilities. On January 1, 2009, the Company adopted the provisions of FAS 157 for non-financial assets and non-financial liabilities that are recognized and disclosed at fair value on a nonrecurring basis. FAS 157 defines fair value, provides guidance for measuring fair value and requires certain disclosures. It does not require any new fair value measurements, but rather applies to all other accounting pronouncements that require or permit fair value measurements.

FAS 157 utilizes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The following is a brief description of those three levels:

Level 1: Observable inputs such as quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets or liabilities in active markets and quoted prices for identical or similar assets or liabilities in markets that are not active.

Level 3: Unobservable inputs that reflect the reporting entity's own assumptions.

The Company's financial instruments consist of the following:

Financial instruments recognized at fair value in the statement of financial position

The Company's financial instruments measured at fair value on a recurring basis are summarized below (*in thousands*):

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Financial instruments measured at fair value	Fair Value Hierarchy	As of June 30, 2009		As of December 31, 2008	
		Carrying Value	Fair Value	Carrying Value	Fair Value
Cash and cash equivalents	Level 1	\$ 5,935	\$ 5,935	\$ 10,341	\$ 10,341
Cash flow hedging instruments	Level 2	(2,648)	(2,648)	(3,483)	(3,483)

The fair value of cash and cash equivalents approximates their respective carrying value. Cash flow hedging instruments, which are considered over-the-counter derivatives, are also carried at their fair values. The Company's fair value estimate for such derivative instruments incorporates quoted market prices at the balance sheet date from the counter party using significant observable inputs and is considered a level 2 fair value measurement.

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Financial instruments not required to be carried at fair value

In April 2009, the FASB issued FSP FAS 107-1 and APB 28-1, *Interim Disclosures about Fair Value of Financial Instruments*. This FASB Staff Position amends FASB Statement No. 107, *Disclosures about Fair Value of Financial Instruments*, to require disclosures about fair value of financial instruments for interim reporting periods of publicly traded companies as well as in annual financial statements. The Company is required to estimate the fair value of financial instruments when it is practical to do so.

Borrowings under the Company's Revolving Credit Facility are carried at historical cost, adjusted for additional borrowings less principal repayments, which approximates fair value. The Company's Convertible Notes are carried at historical cost, adjusted for repurchases and debt discount. The fair value estimate incorporates quoted market prices at the balance sheet date, which was determined to be approximately \$34.9 million and \$51.4 million as of June 30, 2009 and December 31, 2008, respectively. For investment in receivable portfolios, there is no active market or observable inputs for the fair value estimation. The Company considers it not practical to attempt to estimate the fair value of such financial instruments due to the excessive costs that would be incurred in doing so.

The Company does not have any non-financial assets or liabilities that are measured at fair value.

Note 3: Stock-Based Compensation

On March 9, 2009, the Board of Directors approved an amendment and restatement of the 2005 Stock Incentive Plan (2005 Plan) which was originally adopted on March 30, 2005 for Board members, employees, officers, and executives of, and consultants and advisors to, the Company. The amendment and restatement of the 2005 Plan increased by 2,000,000 shares the maximum number of shares of the Company's common stock that may be issued or subject to awards under the plan, established a new 10-year term for the plan and made certain other amendments. The 2005 Plan was approved by the Company's stockholders on June 9, 2009. The 2005 Plan provides for the granting of incentive stock options, nonqualified stock options, stock appreciation rights, restricted stock, restricted stock units, and performance-based awards to eligible individuals. The 2005 Plan originally authorized an aggregate of 1,500,000 shares of the Company's common stock for awards under the 2005 Plan, plus ungranted shares of stock that were available for future awards under the prior 1999 Equity Participation Plan (1999 Plan). In addition, shares subject to options granted under either the 1999 Plan or the 2005 Plan that terminate or expire without being exercised are available for grant under the 2005 Plan. The benefits provided under these plans are share-based compensation subject to the provisions of Statement of Financial Accounting Standard No. 123R, *Share-Based Payment* (FAS 123R).

In accordance with FAS 123R, compensation expense is recognized only for those shares expected to vest, net of estimated forfeitures based on the Company's historical experience and future expectations. For the six months ended June 30, 2009, approximately \$2.1 million was recognized as stock-based compensation expense.

The Company's stock-based compensation arrangements are described below:

Stock Options

The 2005 Plan permits the granting of stock options to certain employees and directors of the Company. Option awards are generally granted with an exercise price equal to the market price of the Company's stock at the date of issuance. Options generally vest based on three to five years of continuous service and have ten-year contractual terms.

The Company uses the Black-Scholes option-pricing model to determine the fair-value of stock-based awards. All options are amortized ratably over the requisite service periods of the awards, which are generally the vesting periods.

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The fair value of options granted is estimated at the date of grant using a Black-Scholes option-pricing model with the following weighted-average assumptions (there were no options granted during the six months ended June 30, 2008):

	Six Months Ended June 30, 2009	Six Months Ended June 30, 2008
Weighted average fair value of options granted	\$ 1.36	
Risk free interest rate	1.9%	
Dividend yield	0.0%	
Volatility factor of the expected market price of the Company's common stock	52.8%	
Weighted-average expected life of options	5 Years	

Unrecognized estimated compensation cost related to stock options as of June 30, 2009, was \$1.5 million, which is expected to be recognized over a weighted-average period of approximately 2.0 years.

A summary of the Company's stock option activity and related information is as follows for the six months ended June 30, 2009:

	Number of Shares	Option Price Per Share	Weighted Average Exercise Price	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2008	2,139,503	\$ 0.35 - \$20.09	\$ 9.14	
Granted	262,500	2.89	2.89	
Cancelled/forfeited	(72,000)	10.92 - 16.19	12.28	
Exercised	(10,000)	2.95	2.95	
Outstanding at June 30, 2009	2,320,003	\$ 0.35 - \$20.09	\$ 8.33	\$ 13,012
Exercisable at June 30, 2009	1,620,506	\$ 0.35 - \$20.09	\$ 8.31	\$ 9,598

The total intrinsic value of options exercised during the six months ended June 30, 2009 and 2008 remained consistent at \$0.1 million. As of June 30, 2009, the weighted-average remaining contractual life of options outstanding and options exercisable was 5.75 years and 4.35 years, respectively.

Restricted Stock Units

Under the Company's 2005 Plan, certain employees and directors are eligible to receive restricted stock units. In accordance with FAS 123R, the fair value of restricted stock units is equal to the closing price of the Company's common stock on the date of issuance. The total number of restricted stock unit awards expected to vest is adjusted by estimated forfeiture rates. As of June 30, 2009, 106,500 of the non-vested shares are expected to vest over approximately three to five years based on certain performance goals (Performance-Based Awards). The fair value of the Performance-Based Awards is expensed over the expected vesting period based on our forfeiture assumptions. If performance goals are not expected to be met, the compensation expense previously recognized would be reversed. No reversals of compensation expense related to the Performance-Based Awards have been made as of June 30, 2009. The remaining 617,540 non-vested shares are not performance-based, and will vest and are being expensed over approximately two to five years of continuous service.

For the six months ended June 30, 2009, restricted stock unit activity and related information are as follows:

Restricted Stock Units	Non-Vested Shares	Weighted Average Grant Date Fair Value
Non-vested at December 31, 2008	628,752	\$ 11.18

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Awarded	224,714	\$	4.20
Vested	(115,846)	\$	10.92
Cancelled/forfeited	(13,580)	\$	10.96
Non-vested at June 30, 2009	724,040	\$	9.06

Unrecognized estimated compensation cost related to restricted stock units as of June 30, 2009, was \$3.3 million, which is expected to be recognized over a weighted-average period of approximately 2.3 years. The fair value of restricted stock units vested for the six months ended June 30, 2009 and 2008 was \$1.0 million and \$0.2 million, respectively.

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In accordance with the provisions of SOP 03-3, discrete receivable portfolio purchases during a quarter are aggregated into pools based on common risk characteristics. Once a static pool is established, the portfolios are permanently assigned to the pool. The discount (*i.e.*, the difference between the cost of each static pool and the related aggregate contractual receivable balance) is not recorded because the Company expects to collect a relatively small percentage of each static pool's contractual receivable balance. As a result, receivable portfolios are recorded at cost at the time of acquisition. All portfolios with common risk characteristics purchased prior to the adoption of SOP 03-3 in the first quarter of 2005 were aggregated by quarter of purchase.

In compliance with SOP 03-3, the Company accounts for its investments in consumer receivable portfolios using either the interest method or the cost recovery method. The interest method applies an effective interest rate, or IRR, to the cost basis of the pool, which remains unchanged throughout the life of the pool, unless there is an increase in subsequent, expected cash flows. Subsequent increases in expected cash flows are generally recognized prospectively through an upward adjustment of the pool's IRR over its remaining life. Subsequent decreases in expected cash flows do not change the IRR, but are recognized as an impairment of the cost basis of the pool, and are reflected in the consolidated statements of income as a reduction in revenue, with a corresponding valuation allowance, offsetting the investment in receivable portfolios in the consolidated statements of financial condition.

The Company accounts for each static pool as a unit for the economic life of the pool (similar to one loan) for recognition of revenue from receivable portfolios, for collections applied to the cost basis of receivable portfolios and for provision for loss or impairment. Revenue from receivable portfolios is accrued based on each pool's IRR applied to each pool's adjusted cost basis. The cost basis of each pool is increased by revenue earned and decreased by gross collections and impairments.

If the amount and timing of future cash collections on a pool of receivables are not reasonably estimable, the Company accounts for such portfolios on the cost recovery method as Cost Recovery Portfolios. The accounts in these portfolios have different risk characteristics than those included in other portfolios acquired during the same quarter, or the necessary information was not available to estimate future cash flows and, accordingly, they were not aggregated with other portfolios. Under the cost recovery method of accounting, no income is recognized until the purchase price of a Cost Recovery Portfolio has been fully recovered. As of June 30, 2009, there were five portfolios accounted for using the cost recovery method, consisting of \$0.6 million in net book value of investment in receivable portfolios, representing all of the healthcare portfolios that the Company had acquired. In September 2007, the Company decided to exit its healthcare purchasing and collection activities. At that time, the Company anticipated either selling these healthcare portfolios or placing the underlying accounts with external agencies for collections. The Company no longer anticipates a sale of these receivable portfolios and has placed them with external collection agencies. Since the Company is no longer actively collecting on these accounts internally, it has classified them as Cost Recovery Portfolios. The \$0.6 million net book value reflects the value the Company expects to realize through the collection activities of the external agencies.

Accretable yield represents the amount of revenue the Company expects to generate over the remaining life of its existing investment in receivable portfolios based on estimated future cash flows. Total accretable yield is the difference between future estimated collections and the current carrying value of a portfolio. All estimated cash flows on portfolios where the cost basis has been fully recovered are classified as zero basis cash flows.

The following tables summarize the Company's accretable yield and an estimate of future zero basis cash flows at the beginning and end of the current period (*in thousands*):

	Six Months Ended June 30, 2009		
	Accretable Yield	Estimate of Zero Basis Cash Flows	Total
Beginning balance at December 31, 2008	\$ 592,825	\$ 8,337	\$ 601,162
Revenue recognized, net	(69,775)	(2,500)	(72,275)
Additions on existing portfolios	5,715	1,032	6,747
Additions for current purchases	81,917		81,917
Balance at March 31, 2009	\$ 610,682	\$ 6,869	\$ 617,551
Revenue recognized, net	(71,576)	(2,389)	(73,965)

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(Reductions) additions on existing portfolios	(15,399)	2,614	(12,785)
Additions for current purchases	106,771		106,771
Balance at June 30, 2009	\$ 630,478	\$ 7,094	\$ 637,572

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	Six Months Ended June 30, 2008		
	Accretible Yield	Estimate of Zero Basis Cash Flows	Total
Beginning balance at December 31, 2007	\$ 486,652	\$ 13,002	\$ 499,654
Revenue recognized, net	(61,510)	(2,558)	(64,068)
Reductions on existing portfolios	(50,898)	(1,015)	(51,913)
Additions for 12 months curve extension	67,287		67,287
Additions for current purchases	112,780		112,780
 Balance at March 31, 2008	 \$ 554,311	 \$ 9,429	 \$ 563,740
Revenue recognized, net	(63,652)	(2,623)	(66,275)
(Reductions) additions on existing portfolios	(3,206)	1,598	(1,608)
Additions for current purchases	79,159		79,159
 Balance at June 30, 2008	 \$ 566,612	 \$ 8,404	 \$ 575,016

During the three months ended June 30, 2009, the Company purchased receivable portfolios with a face value of \$1.9 billion for \$82.0 million, or a purchase cost of 4.2% of face value. The estimated future collections at acquisition for these portfolios amounted to \$203.3 million. During the six months ended June 30, 2009, the Company purchased receivable portfolios with a face value of \$3.3 billion for \$137.9 million, or a purchase cost of 4.2% of face value. The estimated future collections at acquisition for these portfolios amounted to \$341.6 million.

All collections realized after the net book value of a portfolio has been fully recovered (Zero Basis Portfolios) are recorded as revenue (Zero Basis Revenue). During the three months ended June 30, 2009 and 2008, approximately \$2.4 million and \$2.6 million were recognized as Zero Basis Revenue, respectively. During the six months ended June 30, 2009 and 2008, approximately \$4.9 million and \$5.1 million were recognized as Zero Basis Revenue, respectively.

During the quarter ended March 31, 2008, the Company revised the forecasting methodology it used to value a portfolio by extending the collection forecast from 72 months to 84 months. This change was made as a result of the Company's increased confidence in its ability to forecast future cash collections to 84 months. Extending the collection forecast from 72 months to 84 months resulted in an increase in the aggregate total estimated remaining collections for the receivable portfolios, as of March 31, 2008, by \$67.3 million, or 7.5%. The impact of the change in estimate resulted in an increase in net income of \$1.9 million, and an increase in fully diluted earnings per share of \$0.08, for the quarter ended March 31, 2008.

The following tables summarize the changes in the balance of the investment in receivable portfolios during the following periods (*in thousands, except percentages*):

	For the Three Months Ended June 30, 2009			Total
	Accrual Basis Portfolios	Cost Recovery Portfolios	Zero Basis Portfolios	
Balance, beginning of period	\$ 472,875	\$ 609	\$	\$ 473,484
Purchases of receivable portfolios	82,033			82,033
Gross collections ⁽¹⁾	(119,823)	(56)	(2,389)	(122,268)
Put-backs and recalls ⁽²⁾	(506)			(506)
Revenue recognized	76,172		2,357	78,529
Impairment, net	(4,596)		32	(4,564)
 Balance, end of period	 \$ 506,155	 \$ 553	 \$	 \$ 506,708
 Revenue as a percentage of collections ⁽³⁾	 63.6%	 0.0%	 98.7%	 64.2%

For the Three Months Ended June 30, 2008

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	Accrual Basis Portfolios	Cost Recovery Portfolios	Zero Basis Portfolios	Total
Balance, beginning of period	\$ 396,775	\$ 1,432	\$	\$ 398,207
Purchases of receivable portfolios	52,492			52,492
Gross collections ⁽¹⁾	(99,306)	(131)	(2,623)	(102,060)
Put-backs and recalls ⁽²⁾	(357)	2		