

CREDIT ACCEPTANCE CORP
Form 10-Q
October 29, 2018

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q
(Mark One)

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

For the quarterly period ended September 30, 2018

OR

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

For the transition period from _____ to _____

Commission file number 000-20202

CREDIT ACCEPTANCE CORPORATION

(Exact name of registrant as specified in its charter)

Michigan

(State or other jurisdiction of incorporation or organization)

38-1999511

(I.R.S. Employer Identification No.)

25505 W. Twelve Mile Road

Southfield, Michigan

(Address of principal executive offices)

248-353-2700

(Registrant's

telephone

number,

including area

code)

Not Applicable

(Former name,

former address

and former

fiscal year, if

changed since

last report)

48034-8339

(Zip Code)

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The number of shares of Common Stock, \$0.01 par value, outstanding on October 22, 2018 was 19,309,495.

Table of Contents

TABLE OF CONTENTS

PART I. — FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Consolidated Balance Sheets - As of September 30, 2018 and December 31, 2017 1

Consolidated Statements of Income - Three and nine months ended September 30, 2018 and 2017 2

Consolidated Statements of Comprehensive Income - Three and nine months ended September 30, 2018 and 2017 3

Consolidated Statements of Cash Flows - Nine months ended September 30, 2018 and 2017 4

Notes to Consolidated Financial Statements 5

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS 41

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK 56

ITEM 4. CONTROLS AND PROCEDURES 56

PART II. — OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS 57

ITEM 6. EXHIBITS 58

SIGNATURES 59

Table of Contents

PART I. - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CREDIT ACCEPTANCE CORPORATION
CONSOLIDATED BALANCE SHEETS
(UNAUDITED)

(Dollars in millions, except per share data)

	As of	
	September 30, 2018	December 31, 2017
ASSETS:		
Cash and cash equivalents	\$ 195.7	\$ 8.2
Restricted cash and cash equivalents	347.6	255.6
Restricted securities available for sale	56.7	46.1
Loans receivable	6,005.2	5,049.0
Allowance for credit losses	(447.6)	(429.4)
Loans receivable, net	5,557.6	4,619.6
Property and equipment, net	38.7	20.5
Income taxes receivable	20.2	2.2
Other assets	27.6	33.4
Total Assets	\$6,244.1	\$ 4,985.6
LIABILITIES AND SHAREHOLDERS' EQUITY:		
Liabilities:		
Accounts payable and accrued liabilities	\$ 167.9	\$ 151.7
Revolving secured line of credit	—	13.9
Secured financing	3,320.9	2,514.1
Senior notes	544.0	542.8
Mortgage note	12.0	—
Deferred income taxes, net	235.8	187.4
Income taxes payable	0.2	39.9
Total Liabilities	4,280.8	3,449.8
Commitments and Contingencies - See Note 16		
Shareholders' Equity:		
Preferred stock, \$0.01 par value, 1,000,000 shares authorized, none issued	—	—
Common stock, \$0.01 par value, 80,000,000 shares authorized, 19,309,614 and 19,310,049 shares issued and outstanding as of September 30, 2018 and December 31, 2017, respectively	0.2	0.2
Paid-in capital	152.4	145.5
Retained earnings	1,811.3	1,390.3
Accumulated other comprehensive loss	(0.6)	(0.2)
Total Shareholders' Equity	1,963.3	1,535.8
Total Liabilities and Shareholders' Equity	\$6,244.1	\$ 4,985.6

See accompanying notes to consolidated financial statements.

1

Table of Contents

CREDIT ACCEPTANCE CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(UNAUDITED)

(Dollars in millions, except per share data)	For the Three		For the Nine	
	Months Ended		Months Ended	
	September 30,		September 30,	
	2018	2017	2018	2017
Revenue:				
Finance charges	\$303.0	\$ 259.4	\$863.0	\$ 749.2
Premiums earned	12.2	10.3	34.2	30.9
Other income	16.8	14.2	45.8	42.6
Total revenue	332.0	283.9	943.0	822.7
Costs and expenses:				
Salaries and wages	41.1	33.7	123.3	101.9
General and administrative	14.1	14.2	41.3	42.1
Sales and marketing	16.3	14.2	51.3	43.7
Provision for credit losses	14.0	25.7	39.2	68.0
Interest	41.1	30.5	114.3	88.0
Provision for claims	7.0	5.5	19.5	17.6
Total costs and expenses	133.6	123.8	388.9	361.3
Income before provision for income taxes	198.4	160.1	554.1	461.4
Provision for income taxes	47.4	59.4	132.0	168.3
Net income	\$151.0	\$ 100.7	\$422.1	\$ 293.1
Net income per share:				
Basic	\$7.76	\$ 5.19	\$21.69	\$ 15.01
Diluted	\$7.75	\$ 5.19	\$21.68	\$ 14.99
Weighted average shares outstanding:				
Basic	19,465,562	19,407,344	19,456,389	19,528,175
Diluted	19,473,978	19,415,545	19,472,197	19,547,674

See accompanying notes to consolidated financial statements.

2

Table of Contents

CREDIT ACCEPTANCE CORPORATION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(UNAUDITED)

(In millions)	For the Three		For the Nine	
	Months Ended		Months Ended	
	September 30,		September 30,	
	2018	2017	2018	2017
Net income	\$151.0	\$100.7	\$422.1	\$293.1
Other comprehensive income (loss), net of tax:				
Unrealized gain (loss) on securities, net of tax	—	—	(0.4) 0.2
Other comprehensive income (loss)	—	—	(0.4) 0.2
Comprehensive income	\$151.0	\$100.7	\$421.7	\$293.3

See accompanying notes to consolidated financial statements.

3

Table of Contents

CREDIT ACCEPTANCE CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

(In millions)	For the Nine Months Ended September 30, 2018 2017	
Cash Flows From Operating Activities:		
Net income	\$422.1	\$293.1
Adjustments to reconcile cash provided by operating activities:		
Provision for credit losses	39.2	68.0
Depreciation	3.9	4.7
Amortization	10.0	7.5
Provision for deferred income taxes	48.5	60.5
Stock-based compensation	7.8	8.3
Other	(0.2)	0.1
Change in operating assets and liabilities:		
Increase (decrease) in accounts payable and accrued liabilities	21.0	(2.8)
Increase in income taxes receivable	(18.0)	(3.2)
Decrease in income taxes payable	(39.7)	(23.4)
Decrease in other assets	6.4	1.8
Net cash provided by operating activities	501.0	414.6
Cash Flows From Investing Activities:		
Purchases of restricted securities available for sale	(35.6)	(28.0)
Proceeds from sale of restricted securities available for sale	17.3	23.0
Maturities of restricted securities available for sale	7.2	4.3
Principal collected on Loans receivable	1,949.0	1,657.4
Advances to Dealers	(1,870.2)	(1,467.2)
Purchases of Consumer Loans	(917.0)	(686.7)
Accelerated payments of Dealer Holdback	(41.0)	(35.5)
Payments of Dealer Holdback	(98.0)	(100.8)
Purchases of property and equipment	(22.1)	(6.9)
Net cash used in investing activities	(1,010.4)	(640.4)
Cash Flows From Financing Activities:		
Borrowings under revolving secured line of credit	1,724.7	3,076.7
Repayments under revolving secured line of credit	(1,738.6)	(2,946.2)
Proceeds from secured financing	2,696.6	1,664.5
Repayments of secured financing	(1,886.0)	(1,396.8)
Proceeds from mortgage note	12.0	—
Payments of debt issuance costs	(13.0)	(9.1)
Repurchase of common stock	(2.0)	(123.5)
Other	(4.8)	(0.6)
Net cash provided by financing activities	788.9	265.0
Net increase in cash, cash equivalents, restricted cash and restricted cash equivalents	279.5	39.2
Cash, cash equivalents, restricted cash and restricted cash equivalents beginning of period	263.8	239.3
Cash, cash equivalents, restricted cash and restricted cash equivalents end of period	\$543.3	\$278.5
Supplemental Disclosure of Cash Flow Information:		

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

Cash paid during the period for interest	\$112.0	\$88.9
Cash paid during the period for income taxes	\$136.6	\$132.1

See accompanying notes to consolidated financial statements.

4

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“generally accepted accounting principles” or “GAAP”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The results of operations for interim periods are not necessarily indicative of actual results achieved for full fiscal years. The consolidated balance sheet as of December 31, 2017 has been derived from the audited financial statements at that date but does not include all the information and footnotes required by GAAP for complete financial statements. For further information, refer to the consolidated financial statements and footnotes thereto included in the Annual Report on Form 10-K for the year ended December 31, 2017 for Credit Acceptance Corporation (the “Company”, “Credit Acceptance”, “we”, “our” or “us”).

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

We have evaluated events and transactions occurring subsequent to the consolidated balance sheet date of September 30, 2018 for items that could potentially be recognized or disclosed in these financial statements. We did not identify any items which would require disclosure in or adjustment to the consolidated financial statements.

Reclassification

Certain amounts for prior periods have been reclassified to conform to the current presentation. On January 1, 2018, we adopted Accounting Standards Update 2016-18, which was applied retrospectively and changed the presentation and classification of restricted cash and restricted cash equivalents in our consolidated statements of cash flows. For additional information, see Note 3 to the consolidated financial statements. Additionally, the fair value level of measurement of our revolving secured line of credit as of December 31, 2017 was reclassified from Level 1 to Level 2. For additional information, see Note 4 to the consolidated financial statements.

2. DESCRIPTION OF BUSINESS

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

Without our financing programs, consumers are often unable to purchase vehicles or they purchase unreliable ones. Further, as we report to the three national credit reporting agencies, an important ancillary benefit of our programs is that we provide consumers with an opportunity to improve their lives by improving their credit score and move on to more traditional sources of financing.

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

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

Substantially all of the Consumer Loans assigned to us are made to consumers with impaired or limited credit histories. The following table shows the percentage of Consumer Loans assigned to us with either FICO® scores below 650 or no FICO® scores:

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Consumer Loan Assignment Volume				
Percentage of total unit volume with either FICO® scores below 650 or no FICO® scores	95.2%	95.2%	95.7%	95.7%

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

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

Three Months Ended	Unit Volume		Dollar Volume (1)	
	Dealer Loans	Purchased Loans	Dealer Loans	Purchased Loans
March 31, 2017	73.3%	26.7 %	67.8%	32.2 %
June 30, 2017	72.3%	27.7 %	67.9%	32.1 %
September 30, 2017	71.9%	28.1 %	68.6%	31.4 %
December 31, 2017	72.5%	27.5 %	69.7%	30.3 %
March 31, 2018	70.1%	29.9 %	67.4%	32.6 %
June 30, 2018	69.7%	30.3 %	66.8%	33.2 %
September 30, 2018	69.5%	30.5 %	67.0%	33.0 %

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

Portfolio Program

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

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

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

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

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

If the collections on Consumer Loans from a Dealer's pool are not sufficient to repay the advance balance and any other amounts due to us, the Dealer will not receive Dealer Holdback. Certain events may also result in Dealers forfeiting their rights to Dealer Holdback, including becoming inactive before assigning at least 100 Consumer Loans.

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

6

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

Since typically the combination of the advance and the consumer's down payment provides the Dealer with a cash profit at the time of sale, the Dealer's risk in the Consumer Loan is limited. We cannot demand repayment of the advance from the Dealer except in the event the Dealer is in default of the Dealer servicing agreement. Advances are made only after the consumer and Dealer have signed a Consumer Loan contract, we have received the executed Consumer Loan contract and supporting documentation in either physical or electronic form, and we have approved all of the related stipulations for funding.

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

Purchase Program

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

Program Enrollment

Dealers may enroll in our Portfolio Program by (1) paying an up-front, one-time fee of \$9,850, or (2) agreeing to allow us to retain 50% of their first accelerated Dealer Holdback payment. Access to the Purchase Program is typically only granted to Dealers that meet one of the following:

- received first accelerated Dealer Holdback payment under the Portfolio Program;
- franchise dealership; or
- independent dealership that meets certain criteria upon enrollment.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Business Segment Information

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

Cash, Cash Equivalents, Restricted Cash and Restricted Cash Equivalents

Cash equivalents consist of readily marketable securities with original maturities at the date of acquisition of three months or less. As of September 30, 2018 and December 31, 2017, we had \$194.5 million and \$7.8 million, respectively, in cash and cash equivalents that were not insured by the Federal Deposit Insurance Corporation ("FDIC").

Restricted cash and cash equivalents consist of cash pledged as collateral for secured financings and cash held in a trust for future vehicle service contract claims. As of September 30, 2018 and December 31, 2017, we had \$347.0 million and \$255.1 million, respectively, in restricted cash and cash equivalents that were not insured by the FDIC.

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

The following table provides a reconciliation of cash, cash equivalents, restricted cash and restricted cash equivalents reported in our consolidated balance sheets to the total shown in our consolidated statements of cash flows:

(In millions)

	As of			
	September 30, 2018	December 31, 2017	September 30, 2017	December 31, 2016
Cash and cash equivalents	\$195.7	\$ 8.2	\$ 4.9	\$ 14.6
Restricted cash and cash equivalents	347.6	255.6	273.6	224.7
Total cash, cash equivalents, restricted cash and restricted cash equivalents	\$543.3	\$ 263.8	\$ 278.5	\$ 239.3

7

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

Restricted Securities Available for Sale

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

Loans Receivable and Allowance for Credit Losses

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

- the consumer and Dealer have signed a Consumer Loan contract; and
- we have received the executed Consumer Loan contract and supporting documentation in either physical or electronic form.

For accounting and financial reporting purposes, a Consumer Loan is considered to have been assigned to us after the following has occurred:

- the Consumer Loan has been legally assigned to us; and
- we have made a funding decision and generally have provided funding to the Dealer in the form of either an advance under the Portfolio Program or one-time purchase payment under the Purchase Program.

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

Dealer Loans. Amounts advanced to Dealers for Consumer Loans assigned under the Portfolio Program are recorded as Dealer Loans and are aggregated by Dealer for purposes of recognizing revenue and evaluating impairment. We account for Dealer Loans based on forecasted cash flows instead of contractual cash flows as we do not expect to collect all of the contractually specified amounts due to the credit quality of the underlying Consumer Loans. The outstanding balance of each Dealer Loan included in Loans receivable is comprised of the following:

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

Less:

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

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

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

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

Purchased Loans. Amounts paid to Dealers for Consumer Loans assigned under the Purchase Program are recorded as Purchased Loans and are aggregated into pools based on the month of purchase for purposes of recognizing revenue and evaluating impairment. We account for Purchased Loans based on forecasted cash flows instead of contractual cash flows as we do not expect to collect all of the contractually specified amounts due to the credit quality of the assigned Consumer Loans. The outstanding balance of each Purchased Loan pool included in Loans receivable is comprised of the following:

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

Less:

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

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

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

Under our Portfolio Program, certain events may result in Dealers forfeiting their rights to Dealer Holdback. We transfer the Dealer's outstanding Dealer Loan balance to Purchased Loans in the period this forfeiture occurs. During the fourth quarter of 2017, we enhanced our accounting methodology for transferring loans. Beginning in the fourth quarter of 2017, we:

transfer the related Dealer Loan allowance for credit losses balance to Purchased Loans in the period this forfeiture occurs; and
aggregate these Purchased Loans by Dealer for purposes of recognizing revenue and evaluating impairment.

Prior to the fourth quarter of 2017, we:

reversed the Dealer Loan allowance for credit losses balance through Dealer Loan provision for credit losses and established a new allowance for credit losses in Purchased Loans through Purchased Loan provision for credit losses; and
aggregated these Purchased Loans by month of purchase for purposes of recognizing revenue and evaluating impairment.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

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

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

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

Methodology Changes. For the three and nine months ended September 30, 2018 and 2017, we did not make any methodology changes for Loans that had a material impact on our financial statements.

Reinsurance

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

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

We have consolidated the trust within our financial statements based on our determination of the following:

We have a variable interest in the trust. We have a residual interest in the assets of the trust, which is variable in nature, given that it increases or decreases based upon the actual loss experience of the related service contracts. In addition, VSC Re is required to absorb any losses in excess of the trust's assets.

The trust is a variable interest entity. The trust has insufficient equity at risk as no parties to the trust were required to contribute assets that provide them with any ownership interest.

We are the primary beneficiary of the trust. We control the amount of premiums written and placed in the trust through Consumer Loan assignments under our Programs, which is the activity that most significantly impacts the economic performance of the trust. We have the right to receive benefits from the trust that could potentially be significant. In addition, VSC Re has the obligation to absorb losses of the trust that could potentially be significant.

10

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

New Accounting Updates Adopted During the Current Year

Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118. In March 2018, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2018-05, which amended Accounting Standards Codification (“ASC”) Topic 740 (Income Taxes) for income tax accounting implications of the December 2017 Tax Cuts and Jobs Act (“2017 Tax Act”). ASU 2018-05 is effective for fiscal years, and interim periods, beginning in the reporting period that includes the enactment of the 2017 Tax Act. ASU 2018-05 provides guidance for entities under three scenarios: (1) Measurement of certain income tax effects is complete—an entity must reflect the tax effects of the 2017 Tax Act for which the accounting is complete; (2) Measurement of certain income tax effects can be reasonably estimated—an entity must report provisional amounts for those specific income tax effects of the 2017 Tax Act for which the accounting is incomplete but a reasonable estimate can be determined. Provisional amounts or adjustments to provisional amounts identified in the measurement period, as defined, should be included as an adjustment to tax expense or benefit from continuing operations in the period the amounts are determined; and (3) Measurement of certain income tax effects cannot be reasonably estimated—an entity is not required to report provisional amounts for any specific income tax effects of the 2017 Tax Act for which a reasonable estimate cannot be determined, and would continue to apply ASC Topic 740 based on the provisions of the tax laws that were in effect immediately prior to the enactment of the 2017 Tax Act. Entities would report the provisional amounts of the tax effects of the 2017 Tax Act in the first reporting period in which a reasonable estimate can be determined. ASU 2018-05 further provides that the measurement period is complete when a company's accounting is complete and in no circumstances should the measurement period extend beyond one year from the enactment date of the 2017 Tax Act. An entity may be able to complete the accounting under some provisions of the 2017 Tax Act earlier than others. As a result it may need to apply all three scenarios in determining the accounting for the 2017 Tax Act based on the information that is available. The ultimate impact of the 2017 Tax Act on our consolidated financial statements and related disclosures may differ from our current estimates, possibly materially, due to, among other things, changes in interpretations and assumptions we have made, guidance that may be issued, and other actions we may take as a result of the 2017 Tax Act that differ from those presently contemplated. For additional information, see Note 12 to the consolidated financial statements.

Restricted Cash. In November 2016, the FASB issued ASU 2016-18, which amended ASC Topic 230 (Statement of Cash Flows) and requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. ASU 2016-18 is intended to reduce diversity in practice in how restricted cash or restricted cash equivalents are presented and classified in the statement of cash flows. ASU 2016-18 is effective for fiscal years, and interim periods, beginning after December 15, 2017, with early adoption permitted. The standard required application using a retrospective transition method. The adoption of ASU 2016-18 on January 1, 2018 changed the presentation and classification of restricted cash and restricted cash equivalents in our consolidated statements of cash flows. In addition, since cash and restricted cash are presented on separate lines on our consolidated balance sheets, we enhanced the cash and restricted cash disclosures in our significant accounting policies in Note 3 to the consolidated financial statements to reconcile the totals in our consolidated statement of cash flows to the related line items in our consolidated balance sheets.

The following table reconciles the consolidated statement of cash flows line items impacted by the adoption of this standard on January 1, 2018:

(In millions)

	For the Nine Months Ended September 30, 2017	
	ASU	Previously
	Adjusted 2016-18	Reported
	Adjustment	

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

Decrease (increase) in restricted cash and cash equivalents	\$—	\$ 48.9	\$ (48.9)
Net cash used in investing activities	(640.4)	48.9	(689.3)
Net increase (decrease) in cash, cash equivalents, restricted cash and restricted cash equivalents	39.2	48.9	(9.7)
Cash, cash equivalents, restricted cash and restricted cash equivalents beginning of period	239.3	224.7	14.6
Cash, cash equivalents, restricted cash and restricted cash equivalents end of period	\$278.5	\$ 273.6	\$ 4.9

11

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

Recognition and Measurement of Financial Assets and Financial Liabilities. In January 2016, the FASB issued ASU 2016-01, which revised ASC Topic 825 (Financial Instruments) for the recognition, measurement, presentation and disclosure of financial instruments. ASU 2016-01 makes targeted improvements on how entities account for equity investments, present and disclose financial instruments and measure the valuation allowance on deferred tax assets related to available-for-sale debt securities. ASU 2016-01 is effective for fiscal years, and interim periods, beginning after December 15, 2017, with early adoption not permitted. The adoption of ASU 2016-01 on January 1, 2018 did not have a material impact on our consolidated financial statements.

Revenue from Contracts with Customers. In May 2014, the FASB issued ASU 2014-09, which superseded the revenue recognition requirements of ASC Topic 605 (Revenue Recognition), and most industry-specific guidance. ASU 2014-09 is based on the principle that revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2014-09 also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. ASU 2014-09 is only applicable to our other income source of revenue. Finance charges and premiums earned sources of revenue are outside the scope of this guidance. ASU 2014-09 permits two methods of adoption: retrospectively to each prior reporting period presented (full retrospective method), or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application (modified retrospective method). In August 2015, the FASB issued ASU 2015-14 to defer the effective date of ASU 2014-09 by one year to fiscal years beginning after December 15, 2017. ASU 2015-14 also permits early adoption of ASU 2014-09, but not before the original effective date, which was for fiscal years beginning after December 15, 2016. We adopted ASU 2014-09, as amended by ASU 2015-14, on January 1, 2018 using the modified retrospective method. We assessed the impact of the new guidance by evaluating our contracts, identifying our performance obligations, determining when the performance obligations were satisfied to allow us to recognize revenue and determining the amount of revenue to recognize. As a result of this analysis, we determined that our recognition and measurement of other income will not change. The adoption of ASU 2014-09, as amended by ASU 2015-14, did not impact the timing of our revenue recognition; however it expanded our disclosures related to our other income source of revenue.

New Accounting Updates Not Yet Adopted

Accounting for Costs of Implementing Cloud Computing. In August 2018, the FASB issued ASU 2018-15, which reduces complexity in the accounting for costs of implementing a cloud computing service arrangement. This standard aligns the accounting for implementation costs of hosting arrangements, regardless of whether they convey a license to the hosted software. Under the current guidance, the classification of an arrangement as either a software license or a service contract determines whether or not we capitalize implementation costs. If an arrangement meets the definition of a software license, implementation costs are capitalized. If an arrangement meets the definition of a service contract, implementation costs are expensed as incurred. Under the new guidance, implementation costs will be capitalized regardless of their classification. ASU 2018-15 is effective for fiscal years, and interim periods, beginning after December 15, 2019. Early application is permitted, but we have not yet adopted ASU 2018-15. The adoption of ASU 2018-15 will change how we account for our cloud computing arrangements. However, we do not believe that its adoption will have a material impact on our consolidated financial statements and related disclosures.

Measurement of Credit Losses on Financial Instruments. In June 2016, the FASB issued ASU 2016-13, which included an impairment model (known as the current expected credit loss (“CECL”) model) that is based on expected losses rather than incurred losses. Under the new guidance, an entity recognizes an allowance for credit losses based on the difference between contractual future net cash flows and its estimate of expected future net cash flows. The

new guidance also changes the scope of the special accounting for loans acquired with significant credit deterioration. ASU 2016-13 is effective for fiscal years, and interim periods, beginning after December 15, 2019. Early application is permitted for fiscal years, and interim periods, beginning after December 15, 2018. We believe the adoption of ASU 2016-13 will have a material impact on our consolidated financial statements and related disclosures as it will change our accounting policies for Loans.

Application of CECL to Existing Loans

We believe that Loans outstanding prior to the adoption date would qualify for transition relief under ASU 2016-13 and would be accounted for as purchased financial assets with credit deterioration (“PCD Method”). Under the PCD Method, on the adoption date, we would:

- calculate an effective interest rate based on expected future net cash flows; and
 - increase the Loans receivable and related allowance for credit losses balances by the present value of the difference between contractual future net cash flows and expected future net cash flows discounted at the effective interest rate.
- This “gross-up” would not impact the net carrying amount of Loans (Loans receivable less allowance for credit losses) or net income.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

For each reporting period subsequent to adoption, we would:

- recognize finance charge revenue using the effective interest rate that was calculated on the adoption date based on expected future net cash flows; and
- adjust the allowance for credit losses so that the net carrying amount of each Loan equals the present value of expected future net cash flows discounted at the effective interest rate. The adjustment to the allowance for credit losses would be recognized as either provision for credit losses expense or a reversal of provision for credit losses expense.

Application of CECL to Future Loans

We believe that Consumer Loans assigned subsequent to the adoption of ASU 2016-13 would not qualify for the PCD Method and would be accounted for as originated financial assets (“Originated Method”). While the cash flows we expect to collect at the time of assignment are significantly lower than the contractual cash flows owed to us due to credit quality, our Loans do not qualify for the PCD Method due to the following:

- the assignment of the Consumer Loan occurs a moment after the Consumer Loan is originated by the Dealer, so “a more-than-insignificant deterioration in credit quality since origination” has not occurred; and
- Consumer Loans assigned under the Portfolio Program are considered to be advances under Dealer Loans originated by us rather than Consumer Loans purchased by us.

Under the Originated Method, at the time of assignment, we would:

- calculate the effective interest rate based on contractual future net cash flows; and
- record an allowance for credit losses equal to the difference between the initial balance of the Loan (advance or purchase amount) and the present value of expected future net cash flows discounted at the effective interest rate. The initial allowance for credit losses would be recognized as provision for credit losses expense.

For each reporting period subsequent to assignment, we would:

- recognize finance charge revenue using the effective interest rate that was calculated at the time of assignment based on contractual future net cash flows; and
- adjust the allowance for credit losses so that the net carrying amount of each Loan equals the present value of expected future net cash flows discounted at the effective interest rate. The adjustment to the allowance for credit losses would be recognized as either provision for credit losses expense or a reversal of provision for credit losses expense.

We believe the Originated Method would result in financial reporting that is inconsistent with the economics of our Loans as:

- the effective interest rate would be significantly inflated for contractual amounts that were not expected to be collected at the time of assignment; and
- all expected credit losses, including significant credit losses that were expected at both the time of origination and the time of assignment, would be recognized as provision for credit losses expense, despite the fact that credit losses expected at the time of assignment do not represent an economic loss to us.

The net Loan income (finance charge revenue less provision for credit losses) that we will recognize over the life of a Loan equals the cash we collect from the underlying Consumer Loan less the cash we pay to the Dealer. While the total amount of net Loan income we would recognize over the life of the Loan is not impacted by the new guidance, the timing of when we would recognize this income changes significantly. We believe that recognizing net Loan income on a level-yield basis over the life of the Loan based on expected future net cash flows matches the economics of our business. The Originated Method diverges from economic reality by requiring us to recognize a significant

provision for credit losses at the time of assignment for amounts we never expected to realize and finance charge revenue in subsequent periods that is significantly in excess of our expected yields.

Election of the Fair Value Option for Future Loans

Under ASC 825, Financial Instruments, we have the ability to choose to measure Loans at fair value on an instrument-by-instrument basis at specified election dates, with changes in fair value reported in net income (the fair value option). Dealer Loans are only eligible for fair value election at the time a new active Dealer assigns the first Consumer Loan under the Portfolio Program. All Purchased Loans are eligible for fair value election at the time of assignment. The fair value election may not be revoked once an election is made.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

Given that we believe CECL would result in financial reporting that is inconsistent with the economics of our Loans, we are evaluating the fair value option as an alternative to CECL for future Loans. The fair value of our Loans would be determined by calculating the present value of future expected net cash flows estimated by us utilizing a discount rate based on market participant discount rates for comparable investments. While we believe the fair value option would likely result in financial reporting that approximates the economics of our Loans in a stable rate environment, this option could cause our reported results to be volatile in periods when interest rates are rapidly changing. As a result, we are continuing to evaluate our alternatives with respect to the accounting methods that are or will be available to us.

Leases. In February 2016, the FASB issued ASU 2016-02, which required lessees to recognize a right-of-use asset and related lease liability for leases classified as operating leases at the commencement date that have lease terms of more than 12 months. This ASU retains the classification distinction between finance leases and operating leases. ASU 2016-02 is effective for fiscal years, and interim periods, beginning after December 15, 2018. Early application is permitted, but we have not yet adopted ASU 2016-02. This ASU requires application using a retrospective transition method. The impact on our consolidated balance sheets will be based on the present value of future lease payments, the amount of which will depend upon the population of leases in effect at the date of adoption. As of September 30, 2018, our population of leases consisted of operating leases for office space and office equipment with future minimum lease payments totaling \$5.4 million. We do not expect material changes to the recognition of operating lease expense in our consolidated statements of income.

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

4. FAIR VALUE OF FINANCIAL INSTRUMENTS

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

Cash and Cash Equivalents and Restricted Cash and Cash Equivalents. The carrying amounts approximate their fair value due to the short maturity of these instruments.

Restricted Securities Available for Sale. The fair value of U.S. Government and agency securities and corporate bonds is based on quoted market values in active markets. For asset-backed securities, mortgage-backed securities and commercial paper, we use model-based valuation techniques for which all significant assumptions are observable in the market.

Loans Receivable, net. The fair value is determined by calculating the present value of future net cash flows estimated by us utilizing a discount rate comparable with the rate used to calculate our allowance for credit losses.

Revolving Secured Line of Credit. The fair value is determined by calculating the present value of the debt instrument based on current rates for debt with a similar risk profile and maturity.

Secured Financing. The fair value of our asset-backed secured financings ("Term ABS") is determined using quoted market prices; however, these instruments trade in a market with a low trading volume. For our warehouse facilities, the fair values are determined by calculating the present value of each debt instrument based on current rates for debt with similar risk profiles and maturities.

Senior Notes. The fair value is determined using quoted market prices in an active market.

Mortgage Note. The fair value is determined by calculating the present value of the debt instrument based on current rates for debt with a similar risk profile and maturity.

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

(In millions)

	As of September 30, 2018		As of December 31, 2017	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Assets				
Cash and cash equivalents	\$195.7	\$ 195.7	\$8.2	\$ 8.2
Restricted cash and cash equivalents	347.6	347.6	255.6	255.6
Restricted securities available for sale	56.7	56.7	46.1	46.1
Loans receivable, net	5,557.6	5,650.7	4,619.6	4,741.5
Liabilities				
Revolving secured line of credit	\$—	\$ —	\$13.9	\$ 13.9
Secured financing	3,320.9	3,321.5	2,514.1	2,527.6
Senior notes	544.0	564.9	542.8	569.4
Mortgage note	12.0	12.0	—	—

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

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

- Level 1 Valuation is based upon quoted prices for identical instruments traded in active markets.
- Level 2 Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.
- Level 3 Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates or assumptions that market participants would use in pricing the asset or liability.

The following table provides the level of measurement used to determine the fair value for each of our financial instruments measured or disclosed at fair value:

(In millions)

	As of September 30, 2018			Total Fair Value
	Level 1	Level 2	Level 3	
Assets				
Cash and cash equivalents (1)	\$195.7	\$ —	\$ —	—\$ 195.7
Restricted cash and cash equivalents (1)	347.6	—	—	347.6
Restricted securities available for sale (2)	44.8	11.9	—	56.7
Loans receivable, net (1)	—	—	5,650.7	5,650.7
Liabilities				
Revolving secured line of credit (1)	\$—	\$ —	\$ —	—\$ —
Secured financing (1)	—	3,321.5	—	3,321.5
Senior notes (1)	564.9	—	—	564.9
Mortgage note (1)	—	12.0	—	12.0

(In millions)

	As of December 31, 2017			Total Fair Value
	Level 1	Level 2	Level 3	
Assets				
Cash and cash equivalents (1)	\$8.2	\$ —	\$ —	—\$ 8.2
Restricted cash and cash equivalents (1)	255.6	—	—	255.6
Restricted securities available for sale (2)	37.1	9.0	—	46.1
Loans receivable, net (1)	—	—	4,741.5	4,741.5
Liabilities				
Revolving secured line of credit (1)	\$—	\$ 13.9	\$ —	—\$ 13.9

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

Secured financing (1)	—	2,527.6	—	2,527.6
Senior notes (1)	569.4	—	—	569.4

(1) Measured at amortized cost with fair value disclosed.

(2) Measured and recorded at fair value on a recurring basis.

16

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

5. RESTRICTED SECURITIES AVAILABLE FOR SALE

Restricted securities available for sale consist of the following:

(In millions)	As of September 30, 2018			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Corporate bonds	\$23.5	\$ —	—\$ (0.3)	\$ 23.2
U.S. Government and agency securities	22.0	—	(0.4)	21.6
Asset-backed securities	9.7	—	(0.1)	9.6
Mortgage-backed securities	1.4	—	—	1.4
Commercial paper	0.9	—	—	0.9
Total restricted securities available for sale	\$57.5	\$ —	—\$ (0.8)	\$ 56.7

(In millions)	As of December 31, 2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Corporate bonds	\$18.2	\$ —	—\$ (0.1)	\$ 18.1
U.S. Government and agency securities	19.2	—	(0.2)	19.0
Asset-backed securities	6.6	—	—	6.6
Mortgage-backed securities	2.4	—	—	2.4
Total restricted securities available for sale	\$46.4	\$ —	—\$ (0.3)	\$ 46.1

The fair value and gross unrealized losses for restricted securities available for sale, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, are as follows:

(In millions)	Securities Available for Sale with Gross Unrealized Losses as of September 30, 2018					
	Less than 12 Months		12 Months or More		Total Estimated Fair Value	Total Gross Unrealized Losses
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses		
Corporate bonds	\$19.6	\$ (0.3)	\$1.2	\$ —	\$ 20.8	\$ (0.3)
U.S. Government and agency securities	14.6	(0.2)	7.0	(0.2)	21.6	(0.4)
Asset-backed securities	7.0	(0.1)	2.1	—	9.1	(0.1)
Mortgage-backed securities	0.3	—	1.1	—	1.4	—
Commercial paper	0.9	—	—	—	0.9	—
Total restricted securities available for sale	\$42.4	\$ (0.6)	\$11.4	\$ (0.2)	\$ 53.8	\$ (0.8)

(In millions)	Securities Available for Sale with Gross Unrealized Losses as of December 31, 2017					
	Less than 12 Months		12 Months or More		Total	Total
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses		
Corporate bonds	\$18.2	\$ —	\$1.2	\$ —	\$ 18.1	\$ (0.1)
U.S. Government and agency securities	19.2	—	7.0	(0.2)	19.0	(0.2)
Asset-backed securities	6.6	—	2.1	—	6.6	—
Mortgage-backed securities	2.4	—	1.1	—	2.4	—
Total restricted securities available for sale	\$46.4	\$ —	\$11.4	\$ (0.2)	\$ 46.1	\$ (0.2)

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
Corporate bonds	\$11.1	\$ (0.1)	\$1.9	\$ —	\$ 13.0	\$ (0.1)
U.S. Government and agency securities	11.0	(0.1)	7.9	(0.1)	18.9	(0.2)
Asset-backed securities	4.9	—	1.0	—	5.9	—
Mortgage-backed securities	1.2	—	1.2	—	2.4	—
Total restricted securities available for sale	\$28.2	\$ (0.2)	\$12.0	\$ (0.1)	\$ 40.2	\$ (0.3)

17

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

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

(In millions)	As of			
	September 30, 2018		December 31, 2017	
Contractual Maturity	Amortized	Estimated	Amortized	Estimated
	Cost	Fair Value	Cost	Fair Value
Within one year	\$2.5	\$ 2.5	\$2.5	\$ 2.5
Over one year to five years	53.0	52.2	40.5	40.2
Over five years to ten years	0.6	0.6	1.0	1.0
Over ten years	1.4	1.4	2.4	2.4
Total restricted securities available for sale	\$57.5	\$ 56.7	\$46.4	\$ 46.1

6. LOANS RECEIVABLE

Loans receivable consists of the following:

(In millions)	As of September 30, 2018		
	Dealer Loans	Purchased Loans	Total
Loans receivable	\$4,030.2	\$1,975.0	\$6,005.2
Allowance for credit losses	(373.0)	(74.6)	(447.6)
Loans receivable, net	\$3,657.2	\$1,900.4	\$5,557.6

(In millions)	As of December 31, 2017		
	Dealer Loans	Purchased Loans	Total
Loans receivable	\$3,518.1	\$1,530.9	\$5,049.0
Allowance for credit losses	(366.0)	(63.4)	(429.4)
Loans receivable, net	\$3,152.1	\$1,467.5	\$4,619.6

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

A summary of changes in Loans receivable is as follows:

(In millions)	For the Three Months Ended		
	September 30, 2018		
	Dealer	Purchased	Total
	Loans	Loans	
Balance, beginning of period	\$3,918.4	\$1,861.7	\$5,780.1
New Consumer Loan assignments (1)	556.7	274.3	831.0
Principal collected on Loans receivable	(466.0)	(181.3)	(647.3)
Accelerated Dealer Holdback payments	11.6	—	11.6
Dealer Holdback payments	31.9	—	31.9
Transfers (2)	(20.2)	20.2	—
Write-offs	(2.5)	(0.2)	(2.7)
Recoveries (3)	0.3	0.3	0.6
Balance, end of period	\$4,030.2	\$1,975.0	\$6,005.2

(In millions)	For the Three Months Ended		
	September 30, 2017		
	Dealer	Purchased	Total
	Loans	Loans	
Balance, beginning of period	\$3,385.3	\$1,252.4	\$4,637.7
New Consumer Loan assignments (1)	474.0	216.6	690.6
Principal collected on Loans receivable	(424.6)	(116.5)	(541.1)
Accelerated Dealer Holdback payments	11.9	—	11.9
Dealer Holdback payments	32.1	—	32.1
Transfers (2)	(1.9)	1.9	—
Write-offs	(2.9)	(1.2)	(4.1)
Recoveries (3)	0.4	0.1	0.5
Balance, end of period	\$3,474.3	\$1,353.3	\$4,827.6

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

(In millions)	For the Nine Months Ended		
	September 30, 2018		
	Dealer Loans	Purchased Loans	Total
Balance, beginning of period	\$3,518.1	\$1,530.9	\$5,049.0
New Consumer Loan assignments (1)	1,870.2	917.0	2,787.2
Principal collected on Loans receivable	(1,425.2)	(523.8)	(1,949.0)
Accelerated Dealer Holdback payments	41.0	—	41.0
Dealer Holdback payments	98.0	—	98.0
Transfers (2)	(53.3)	53.3	—
Write-offs	(21.3)	(3.2)	(24.5)
Recoveries (3)	2.7	0.8	3.5
Balance, end of period	\$4,030.2	\$1,975.0	\$6,005.2

(In millions)	For the Nine Months Ended		
	September 30, 2017		
	Dealer Loans	Purchased Loans	Total
Balance, beginning of period	\$3,209.0	\$998.0	\$4,207.0
New Consumer Loan assignments (1)	1,467.2	686.7	2,153.9
Principal collected on Loans receivable	(1,323.8)	(333.6)	(1,657.4)
Accelerated Dealer Holdback payments	35.5	—	35.5
Dealer Holdback payments	100.8	—	100.8
Transfers (2)	(4.1)	4.1	—
Write-offs	(11.4)	(2.1)	(13.5)
Recoveries (3)	1.1	0.2	1.3
Balance, end of period	\$3,474.3	\$1,353.3	\$4,827.6

The Dealer Loans amount represents advances paid to Dealers on Consumer Loans assigned under our Portfolio (1) Program. The Purchased Loans amount represents one-time payments made to Dealers to purchase Consumer Loans assigned under our Purchase Program.

(2) Under our Portfolio Program, certain events may result in Dealers forfeiting their rights to Dealer Holdback. We transfer the Dealer's outstanding Dealer Loan balance to Purchased Loans in the period this forfeiture occurs.

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

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

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

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

(In millions)	For the Three Months Ended		
	September 30, 2018		
	Dealer Loans	Purchased Loans	Total
Balance, beginning of period	\$1,246.6	\$ 708.4	\$1,955.0
New Consumer Loan assignments (1)	227.8	112.6	340.4
Accretion (2)	(208.6)	(96.6)	(305.2)
Provision for credit losses	12.4	1.6	14.0
Forecast changes	(0.1)	17.2	17.1
Transfers (3)	(7.8)	10.2	2.4
Balance, end of period	\$1,270.3	\$ 753.4	\$2,023.7

(In millions)	For the Three Months Ended		
	September 30, 2017		
	Dealer Loans	Purchased Loans	Total
Balance, beginning of period	\$1,038.4	\$ 456.4	\$1,494.8
New Consumer Loan assignments (1)	192.6	92.7	285.3
Accretion (2)	(194.7)	(67.0)	(261.7)
Provision for credit losses	20.2	5.5	25.7
Forecast changes	(1.9)	7.4	5.5
Transfers (3)	(0.5)	1.3	0.8
Balance, end of period	\$1,054.1	\$ 496.3	\$1,550.4

(In millions)	For the Nine Months Ended		
	September 30, 2018		
	Dealer Loans	Purchased Loans	Total
Balance, beginning of period	\$1,088.6	\$ 576.9	\$1,665.5
New Consumer Loan assignments (1)	768.1	380.2	1,148.3
Accretion (2)	(603.5)	(266.1)	(869.6)
Provision for credit losses	34.3	4.9	39.2
Forecast changes	3.5	31.0	34.5
Transfers (3)	(20.7)	26.5	5.8
Balance, end of period	\$1,270.3	\$ 753.4	\$2,023.7

(In millions)	For the Nine Months Ended		
	September 30, 2017		
	Dealer Loans	Purchased Loans	Total
Balance, beginning of period	\$982.6	\$ 348.1	\$1,330.7
New Consumer Loan assignments (1)	599.1	284.6	883.7
Accretion (2)	(575.5)	(180.3)	(755.8)
Provision for credit losses	55.6	12.4	68.0

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

Forecast changes	(6.8) 29.2	22.4
Transfers (3)	(0.9) 2.3	1.4
Balance, end of period	\$1,054.1	\$ 496.3	\$1,550.4

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

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

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

(In millions)	For the Three Months Ended September 30, 2018		
	Dealer Loans	Purchased Loans	Total
Contractual net cash flows at the time of assignment (1)	\$883.1	\$606.1	\$1,489.2
Expected net cash flows at the time of assignment (2)	784.5	386.9	1,171.4
Fair value at the time of assignment (3)	556.7	274.3	831.0

(In millions)	For the Three Months Ended September 30, 2017		
	Dealer Loans	Purchased Loans	Total
Contractual net cash flows at the time of assignment (1)	\$754.6	\$476.0	\$1,230.6
Expected net cash flows at the time of assignment (2)	666.6	309.3	975.9
Fair value at the time of assignment (3)	474.0	216.6	690.6

(In millions)	For the Nine Months Ended September 30, 2018		
	Dealer Loans	Purchased Loans	Total
Contractual net cash flows at the time of assignment (1)	\$2,965.7	\$2,028.4	\$4,994.1
Expected net cash flows at the time of assignment (2)	2,638.3	1,297.2	3,935.5
Fair value at the time of assignment (3)	1,870.2	917.0	2,787.2

(In millions)	For the Nine Months Ended September 30, 2017		
	Dealer Loans	Purchased Loans	Total
Contractual net cash flows at the time of assignment (1)	\$2,335.1	\$1,492.0	\$3,827.1
Expected net cash flows at the time of assignment (2)	2,066.3	971.3	3,037.6
Fair value at the time of assignment (3)	1,467.2	686.7	2,153.9

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

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

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

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

Credit Quality

We monitor and evaluate the credit quality of Consumer Loans assigned under our Portfolio and Purchase Programs on a monthly basis by comparing our current forecasted collection rates to our initial expectations. For additional information regarding credit quality, see Note 3 to the consolidated financial statements. The following table compares our forecast of Consumer Loan collection rates as of September 30, 2018, with the forecasts as of June 30, 2018, December 31, 2017 and at the time of assignment, segmented by year of assignment:

Consumer Loan Assignment Year	Forecasted Collection Percentage as of (1)				Current Forecast Variance from			
	September 30, 2018		December 31, 2017	Initial Forecast	June 30, 2018	December 31, 2017	Initial Forecast	
	2018	2018						
2009	79.5%	79.5%	79.5%	% 71.9%	0.0%	0.0%	% 7.6%	%
2010	77.7%	77.7%	77.6%	% 73.6%	0.0%	0.1%	% 4.1%	%
2011	74.7%	74.8%	74.7%	% 72.5%	-0.1%	0.0%	% 2.2%	%
2012	73.8%	73.8%	73.8%	% 71.4%	0.0%	0.0%	% 2.4%	%
2013	73.5%	73.5%	73.5%	% 72.0%	0.0%	0.0%	% 1.5%	%
2014	71.7%	71.7%	71.7%	% 71.8%	0.0%	0.0%	% -0.1%	%
2015	65.4%	65.4%	65.5%	% 67.7%	0.0%	-0.1%	% -2.3%	%
2016	64.3%	64.4%	64.8%	% 65.4%	-0.1%	-0.5%	% -1.1%	%
2017	65.6%	65.6%	65.6%	% 64.0%	0.0%	0.0%	% 1.6%	%
2018 (2)	64.8%	64.5%	—	% 63.6%	0.3%	—	% 1.2%	%

Represents the total forecasted collections we expect to collect on the Consumer Loans as a percentage of the repayments that we were contractually owed on the Consumer Loans at the time of assignment. Contractual (1) repayments include both principal and interest. Forecasted collection rates are negatively impacted by canceled Consumer Loans as the contractual amount owed is not removed from the denominator for purposes of computing forecasted collection rates in the table.

The forecasted collection rate for 2018 Consumer Loans as of September 30, 2018 includes both Consumer Loans (2) that were in our portfolio as of June 30, 2018 and Consumer Loans assigned during the most recent quarter. The following table provides forecasted collection rates for each of these segments:

2018 Consumer Loan Assignment Period	Forecasted Collection Percentage as of			Current Forecast Variance from	
	September 30, 2018		Initial Forecast	June 30, 2018	Initial Forecast
	2018	2018			
January 1, 2018 through June 30, 2018	65.3%	64.5%	% 63.6%	0.8%	1.7%
July 1, 2018 through September 30, 2018	63.8%	—	% 63.5%	—	0.3%

Consumer Loans assigned in 2009 through 2013, 2017 and 2018 have yielded forecasted collection results materially better than our initial estimates, while Consumer Loans assigned in 2015 and 2016 have yielded forecasted collection results materially worse than our initial estimates. For Consumer Loans assigned in 2014, actual results have been close to our initial estimates. For the three months ended September 30, 2018, forecasted collection rates improved for Consumer Loans assigned in 2018 and were generally consistent with expectations at the start of the period for all other assignment years presented. For the nine months ended September 30, 2018, forecasted collection rates improved for Consumer Loans assigned in 2018, declined for Consumer Loans assigned in 2016 and were generally

consistent with expectations at the start of the period for all other assignment years presented.

23

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

Advances paid to Dealers on Consumer Loans assigned under our Portfolio Program and one-time payments made to Dealers to purchase Consumer Loans assigned under our Purchase Program are aggregated into pools for purposes of recognizing revenue and evaluating impairment. As a result of this aggregation, we are not able to segment the carrying amounts of the majority of our Loan portfolio by year of assignment. We are able to segment our Loan portfolio by the performance of the Loan pools. Performance considers both the amount and timing of expected net cash flows and is measured by comparing the balance of the Loan pool to the discounted value of the expected future net cash flows of each Loan pool using the yield established at the time of assignment. The following table segments our Loan portfolio by the performance of the Loan pools:

(In millions)	As of September 30, 2018					
	Loan Pool Performance Meets or Exceeds Initial Estimates			Loan Pool Performance Less than Initial Estimates		
	Dealer Loans	Purchased Loans	Total	Dealer Loans	Purchased Loans	Total
Loans receivable	\$1,237.0	\$1,276.0	\$2,513.0	\$2,793.2	\$699.0	\$3,492.2
Allowance for credit losses	—	—	—	(373.0)	(74.6)	(447.6)
Loans receivable, net	\$1,237.0	\$1,276.0	\$2,513.0	\$2,420.2	\$624.4	\$3,044.6

(In millions)	As of December 31, 2017					
	Loan Pool Performance Meets or Exceeds Initial Estimates			Loan Pool Performance Less than Initial Estimates		
	Dealer Loans	Purchased Loans	Total	Dealer Loans	Purchased Loans	Total
Loans receivable	\$755.2	\$472.7	\$1,227.9	\$2,762.9	\$1,058.2	\$3,821.1
Allowance for credit losses	—	—	—	(366.0)	(63.4)	(429.4)
Loans receivable, net	\$755.2	\$472.7	\$1,227.9	\$2,396.9	\$994.8	\$3,391.7

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

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

(In millions)	For the Three Months Ended September 30, 2018		
	Dealer Loans	Purchased Loans	Total
Balance, beginning of period	\$365.9	\$ 69.8	\$435.7
Provision for credit losses	12.4	1.6	14.0
Transfers (1)	(3.1)	3.1	—
Write-offs	(2.5)	(0.2)	(2.7)
Recoveries (2)	0.3	0.3	0.6
Balance, end of period	\$373.0	\$ 74.6	\$447.6

(In millions)	For the Three Months Ended September 30, 2017		
	Dealer Loans	Purchased Loans	Total
Balance, beginning of period	\$336.9	\$ 17.2	\$354.1
Provision for credit losses	20.2	5.5	25.7
Write-offs	(2.9)	(1.2)	(4.1)
Recoveries (2)	0.4	0.1	0.5
Balance, end of period	\$354.6	\$ 21.6	\$376.2

(In millions)	For the Nine Months Ended September 30, 2018		
	Dealer Loans	Purchased Loans	Total
Balance, beginning of period	\$366.0	\$ 63.4	\$429.4
Provision for credit losses	34.3	4.9	39.2
Transfers (1)	(8.7)	8.7	—
Write-offs	(21.3)	(3.2)	(24.5)
Recoveries (2)	2.7	0.8	3.5
Balance, end of period	\$373.0	\$ 74.6	\$447.6

(In millions)	For the Nine Months Ended September 30, 2017		
	Dealer Loans	Purchased Loans	Total
Balance, beginning of period	\$309.3	\$ 11.1	\$320.4
Provision for credit losses	55.6	12.4	68.0
Write-offs	(11.4)	(2.1)	(13.5)
Recoveries (2)	1.1	0.2	1.3
Balance, end of period	\$354.6	\$ 21.6	\$376.2

Under our Portfolio Program, certain events may result in Dealers forfeiting their rights to Dealer Holdback.

- (1) We transfer the Dealer's outstanding Dealer Loan balance to Purchased Loans in the period this forfeiture occurs. Beginning in the fourth quarter of 2017, we also transfer the related allowance for credit losses balance to Purchased Loans in the period this forfeiture occurs.

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

25

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

7. PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

(In millions)	As of	
	September 30, 2018	December 31, 2017
Land and land improvements	\$2.6	\$ 2.5
Building and improvements	31.8	15.6
Data processing equipment and software	36.5	31.3
Office furniture and equipment	3.8	3.8
Leasehold improvements	2.2	2.2
Total property and equipment	76.9	55.4
Less: Accumulated depreciation on property and equipment	(38.2)	(34.9)
Total property and equipment, net	\$38.7	\$ 20.5

8. REINSURANCE

A summary of reinsurance activity is as follows:

(In millions)	For the Three Months Ended September 30, 2018		For the Nine Months Ended September 30, 2017	
Net assumed written premiums	\$12.9	\$9.7	\$43.3	\$31.6
Net premiums earned	12.2	10.3	34.2	30.9
Provision for claims	7.0	5.5	19.5	17.6
Amortization of capitalized acquisition costs	0.3	0.3	0.8	0.8

The trust assets and related reinsurance liabilities are as follows:

(In millions)	Balance Sheet location	As of	
		September 30, 2018	December 31, 2017
Trust assets	Restricted cash and cash equivalents	\$ 0.7	\$ 0.8
Trust assets	Restricted securities available for sale	56.7	46.1
Unearned premium	Accounts payable and accrued liabilities	43.2	34.1
Claims reserve (1)	Accounts payable and accrued liabilities	1.7	1.0

(1) The claims reserve represents our liability for incurred-but-not-reported claims and is estimated based on historical claims experience.

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

9. OTHER INCOME

Other income consists of the following:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
(In millions)	2018	2017	2018	2017
Ancillary product profit sharing	\$8.7	\$6.2	\$20.9	\$16.6
Remarketing fees	2.8	2.8	8.9	8.7
GPS-SID fees	1.4	2.3	5.3	9.0
Dealer support products and services	1.0	1.2	3.4	3.7
Dealer enrollment fees	1.0	1.0	3.3	3.0
Other	1.9	0.7	4.0	1.6
Total	\$16.8	\$14.2	\$45.8	\$42.6

Ancillary product profit sharing consists of payments received from Third Party Providers (“TPPs”) based upon the performance of vehicle service contracts and Guaranteed Asset Protection (“GAP”) contracts, and are recognized as income over the life of the vehicle service contracts and GAP contracts.

Remarketing fees consist of fees retained from the sale of repossessed vehicles by Vehicle Remarketing Services, Inc. (“VRS”), our wholly-owned subsidiary that is responsible for remarketing vehicles for Credit Acceptance. VRS coordinates vehicle repossessions with a nationwide network of repossession contractors, the redemption of the vehicles by the consumers, and the sale of the vehicles through a nationwide network of vehicle auctions. VRS recognizes income from the retained fees at the time of the sale and does not retain a fee if a repossessed vehicle is redeemed by the consumer prior to the sale.

GPS-SID fees consist of fees we receive from a TPP for providing Dealers in certain states the ability to purchase GPS Starter Interrupt Devices (“GPS-SID”). Through this program, Dealers can install GPS-SID on vehicles financed by us that can be activated if the consumer fails to make payments on their account, and can result in the prompt repossession of the vehicle. Dealers purchase GPS-SID directly from the TPP and the TPP pays us a vendor fee for each device sold. GPS-SID fee income is recognized when the unit is sold.

Dealer support products and services consist of income earned from products and services provided to Dealers to assist with their operations, including sales and marketing, purchasing supplies and materials and acquiring vehicle inventory. Income is recognized in the period the product or service is provided.

Dealer enrollment fees include fees from Dealers that enroll in our Portfolio Program. Depending on the enrollment option selected by the Dealer, Dealers may have enrolled by paying us an upfront, one-time fee, or by agreeing to allow us to retain 50% of their first accelerated Dealer Holdback payment. For additional information regarding program enrollment, see Note 2 to the consolidated financial statements. A portion of the \$9,850 upfront, one-time fee is considered to be Dealer support products and services revenue. The remaining portion of the \$9,850 fee is considered to be a Dealer enrollment fee, which is amortized on a straight-line basis over the estimated life of the Dealer relationship. The 50% portion of the first accelerated Dealer Holdback payment is also considered to be a Dealer enrollment fee. We do not recognize any of this Dealer enrollment fee until the Dealer has met the eligibility

requirements to receive an accelerated Dealer Holdback payment and the amount of the first payment, if any, has been calculated. Once the accelerated Dealer Holdback payment has been calculated, we defer the 50% portion that we keep and recognize it on a straight-line basis over the remaining estimated life of the Dealer relationship.

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

The following table disaggregates our other income by major source of income and timing of the revenue recognition:
(In millions)

	For the Three Months Ended September 30, 2018						
	Ancillary product profit sharing	Remarketing fees	GPS-SID fees	Dealer support products and services	Dealer enrollment fees	Other	Total Other Income
Source of income							
Third Party Providers	\$8.7	\$ —	\$ 1.4	\$ —	\$ —	\$ 1.9	\$ 12.0
Dealers	—	2.8	—	1.0	1.0	—	4.8
Total	\$8.7	\$ 2.8	\$ 1.4	\$ 1.0	\$ 1.0	\$ 1.9	\$ 16.8
Timing of revenue recognition							
Over time	\$8.7	\$ —	\$ —	\$ —	\$ 1.0	\$ 1.4	\$ 11.1
At a point in time	—	2.8	1.4	1.0	—	0.5	5.7
Total	\$8.7	\$ 2.8	\$ 1.4	\$ 1.0	\$ 1.0	\$ 1.9	\$ 16.8

(In millions)

	For the Nine Months Ended September 30, 2018						
	Ancillary product profit sharing	Remarketing fees	GPS-SID fees	Dealer support products and services	Dealer enrollment fees	Other	Total Other Income
Source of income							
Third Party Providers	\$20.9	\$ —	\$ 5.3	\$ —	\$ —	\$ 4.0	\$ 30.2
Dealers	—	8.9	—	3.4	3.3	—	15.6
Total	\$20.9	\$ 8.9	\$ 5.3	\$ 3.4	\$ 3.3	\$ 4.0	\$ 45.8
Timing of revenue recognition							
Over time	\$20.9	\$ —	\$ —	\$ —	\$ 3.3	\$ 3.6	\$ 27.8
At a point in time	—	8.9	5.3	3.4	—	0.4	18.0
Total	\$20.9	\$ 8.9	\$ 5.3	\$ 3.4	\$ 3.3	\$ 4.0	\$ 45.8

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

10. DEBT

Debt consists of the following:

(In millions)	As of September 30, 2018			
	Unamortized			
	Principal Debt	Issuance	Unamortized Discount	Carrying Amount
	Outstanding	Costs		
Revolving secured line of credit (1)	\$—	\$ —	\$ —	\$—
Secured financing (2)	3,339.7	(18.8)	—	3,320.9
Senior notes	550.0	(4.8)	(1.2)	544.0
Mortgage note	12.0	—	—	12.0
Total debt	\$3,901.7	\$ (23.6)	\$ (1.2)	\$3,876.9

(In millions)	As of December 31, 2017			
	Unamortized			
	Principal Debt	Issuance	Unamortized Discount	Carrying Amount
	Outstanding	Costs		
Revolving secured line of credit (1)	\$13.9	\$ —	\$ —	\$13.9
Secured financing (2)	2,529.1	(15.0)	—	2,514.1
Senior notes	550.0	(5.9)	(1.3)	542.8
Total debt	\$3,093.0	\$ (20.9)	\$ (1.3)	\$3,070.8

(1) Excludes deferred debt issuance costs of \$3.2 million and \$2.8 million as of September 30, 2018 and December 31, 2017, respectively, which are included in other assets.

(2) Warehouse facilities and Term ABS.

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

General information for each of our financing transactions in place as of September 30, 2018 is as follows:

(Dollars in millions)

Financings	Wholly-owned Subsidiary	Maturity Date	Financing Amount	Interest Rate as of September 30, 2018
Revolving Secured Line of Credit	n/a	06/22/2021	\$350.0(1)	At our option, either LIBOR plus 187.5 basis points or the prime rate plus 87.5 basis points
Warehouse Facility II (2)	CAC Warehouse Funding Corp. II	12/20/2020(3)	400.0	LIBOR plus 175 basis points (4)
Warehouse Facility IV (2)	CAC Warehouse Funding LLC IV	04/30/2020(3)	250.0	LIBOR plus 225 basis points (4)
Warehouse Facility V (2)	CAC Warehouse Funding LLC V	08/17/2021(5)	100.0	LIBOR plus 190 basis points (4)
Warehouse Facility VI (2)	CAC Warehouse Funding LLC VI	09/30/2020(3)	75.0	LIBOR plus 200 basis points
Warehouse Facility VII (2)	CAC Warehouse Funding LLC VII	12/01/2019(6)	150.0	Commercial paper rate plus 190 basis points for class A and plus 220 basis points for class B (4)
Term ABS 2015-2 (2)	Credit Acceptance Funding LLC 2015-2	08/15/2017(3)	300.2	Fixed rate
Term ABS 2016-1 (2)	Credit Acceptance Funding LLC 2016-1	02/15/2018(3)	385.0	LIBOR plus 195 basis points (4)
Term ABS 2016-2 (2)	Credit Acceptance Funding LLC 2016-2	05/15/2018(3)	350.2	Fixed rate
Term ABS 2016-3 (2)	Credit Acceptance Funding LLC 2016-3	10/15/2018(3)	350.0	Fixed rate
Term ABS 2017-1 (2)	Credit Acceptance Funding LLC 2017-1	02/15/2019(3)	350.0	Fixed rate
Term ABS 2017-2 (2)	Credit Acceptance Funding LLC 2017-2	06/17/2019(3)	450.0	Fixed rate
Term ABS 2017-3 (2)	Credit Acceptance Funding LLC 2017-3	10/15/2019(3)	350.0	Fixed rate
Term ABS 2018-1 (2)	Credit Acceptance Funding LLC 2018-1	02/17/2020(3)	500.0	Fixed rate
Term ABS 2018-2 (2)	Credit Acceptance Funding LLC 2018-2	05/15/2020(3)	450.0	Fixed rate
Term ABS 2018-3 (2)	Credit Acceptance Funding LLC 2018-3	08/17/2020(3)	398.3	Fixed rate
2021 Senior Notes	n/a	02/15/2021	300.0	Fixed rate
2023 Senior Notes	n/a	03/15/2023	250.0	Fixed rate
Mortgage Note	Chapter 4 Properties, LLC	08/06/2023	12.0	LIBOR plus 150 basis points

(1)The amount of the facility will decrease to \$315.0 million on June 22, 2019.

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

(3)

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

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

(5) Represents the revolving maturity date. The outstanding balance will amortize after the revolving maturity date and any amounts remaining on August 17, 2023 will be due on that date.

(6) Represents the revolving maturity date. The outstanding balance will amortize after the revolving maturity date and any amounts remaining on November 30, 2021 will be due on that date.

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

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

(In millions)	For the Three		For the Nine	
	Months Ended		Months Ended	
	September 30,		September 30,	
	2018	2017	2018	2017
Revolving Secured Line of Credit				
Maximum outstanding principal balance	\$ 153.9	\$ 130.5	\$ 265.4	\$ 276.7
Average outstanding principal balance	22.2	35.7	44.8	92.2
Warehouse Facility II				
Maximum outstanding principal balance	201.0	—	201.0	263.4
Average outstanding principal balance	4.4	—	4.4	3.4
Warehouse Facility IV				
Maximum outstanding principal balance	—	—	99.0	12.0
Average outstanding principal balance	—	—	0.7	7.8
Warehouse Facility V				
Maximum outstanding principal balance	97.3	—	99.0	100.0
Average outstanding principal balance	2.1	—	1.4	10.4
Warehouse Facility VI				
Maximum outstanding principal balance	—	—	75.0	75.0
Average outstanding principal balance	—	—	0.5	9.8
Warehouse Facility VII				
Maximum outstanding principal balance	100.0	—	150.0	—
Average outstanding principal balance	2.2	—	10.4	—

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

(Dollars in millions)	As of			
	September 30, 2018	December 31, 2017		
Revolving Secured Line of Credit				
Principal balance outstanding	\$—	\$ 13.9		
Amount available for borrowing (1)	350.0	336.1		
Interest rate	—	%	3.44	%
Warehouse Facility II				
Principal balance outstanding	\$—	\$ —		
Amount available for borrowing (1)	400.0	400.0		
Loans pledged as collateral	—	—		
Restricted cash and cash equivalents pledged as collateral	1.4	1.0		
Interest rate	—	%	—	%
Warehouse Facility IV				
Principal balance outstanding	\$—	\$ —		
Amount available for borrowing (1)	250.0	100.0		
Loans pledged as collateral	—	—		
Restricted cash and cash equivalents pledged as collateral	1.3	1.0		
Interest rate	—	%	—	%
Warehouse Facility V				
Principal balance outstanding	\$—	\$ —		
Amount available for borrowing (1)	100.0	100.0		
Loans pledged as collateral	—	—		
Restricted cash and cash equivalents pledged as collateral	1.2	1.0		
Interest rate	—	%	—	%
Warehouse Facility VI				
Principal balance outstanding	\$—	\$ —		
Amount available for borrowing (1)	75.0	75.0		
Loans pledged as collateral	—	—		
Restricted cash and cash equivalents pledged as collateral	0.1	—		
Interest rate	—	%	—	%
Warehouse Facility VII				
Principal balance outstanding	\$—	\$ —		
Amount available for borrowing (1)	150.0	150.0		
Loans pledged as collateral	—	—		
Restricted cash and cash equivalents pledged as collateral	1.4	1.0		
Interest rate	—	%	—	%
Term ABS 2015-1				
Principal balance outstanding	\$—	\$ 78.0		
Loans pledged as collateral	—	238.4		
Restricted cash and cash equivalents pledged as collateral	—	23.3		
Interest rate	—	%	2.88	%
Term ABS 2015-2				
Principal balance outstanding	\$50.4	\$ 215.9		
Loans pledged as collateral	210.7	313.3		
Restricted cash and cash equivalents pledged as collateral	22.4	26.4		

Interest rate

3.31 % 2.72 %

32

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

Term ABS 2016-1			
Principal balance outstanding	\$190.8	\$385.0	
Loans pledged as collateral	363.0	467.2	
Restricted cash and cash equivalents pledged as collateral	32.8	36.6	
Interest rate	4.11	% 3.18	%
Term ABS 2016-2			
Principal balance outstanding	\$250.2	\$350.2	
Loans pledged as collateral	372.5	428.0	
Restricted cash and cash equivalents pledged as collateral	31.6	33.2	
Interest rate	2.99	% 2.83	%
Term ABS 2016-3			
Principal balance outstanding	\$350.0	\$350.0	
Loans pledged as collateral	425.8	425.7	
Restricted cash and cash equivalents pledged as collateral	33.2	31.1	
Interest rate	2.53	% 2.53	%
Term ABS 2017-1			
Principal balance outstanding	\$350.0	\$350.0	
Loans pledged as collateral	431.2	425.9	
Restricted cash and cash equivalents pledged as collateral	33.1	30.8	
Interest rate	2.78	% 2.78	%
Term ABS 2017-2			
Principal balance outstanding	\$450.0	\$450.0	
Loans pledged as collateral	549.5	545.8	
Restricted cash and cash equivalents pledged as collateral	41.4	39.8	
Interest rate	2.72	% 2.72	%
Term ABS 2017-3			
Principal balance outstanding	\$350.0	\$350.0	
Loans pledged as collateral	425.8	482.6	
Restricted cash and cash equivalents pledged as collateral	30.9	29.6	
Interest rate	2.88	% 2.88	%
Term ABS 2018-1			
Principal balance outstanding	\$500.0	\$—	
Loans pledged as collateral	610.1	—	
Restricted cash and cash equivalents pledged as collateral	44.0	—	
Interest rate	3.24	% —	%
Term ABS 2018-2			
Principal balance outstanding	\$450.0	\$—	
Loans pledged as collateral	571.0	—	
Restricted cash and cash equivalents pledged as collateral	39.4	—	
Interest rate	3.68	% —	%
Term ABS 2018-3			
Principal balance outstanding	\$398.3	\$—	
Loans pledged as collateral	570.0	—	
Restricted cash and cash equivalents pledged as collateral	32.7	—	
Interest rate	3.72	% —	%
2021 Senior Notes			
Principal balance outstanding	\$300.0	\$300.0	

Interest rate

6.125 % 6.125 %

33

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

2023 Senior Notes

Principal balance outstanding \$250.0 \$250.0

Interest rate 7.375 % 7.375 %

Mortgage Note

Principal balance outstanding \$12.0 \$—

Interest rate 3.61 % — %

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

Revolving Secured Line of Credit Facility

We have a \$350.0 million revolving secured line of credit facility with a commercial bank syndicate. The amount of the facility will decrease to \$315.0 million on June 22, 2019. Borrowings under the revolving secured line of credit facility, including any letters of credit issued under the facility, are subject to a borrowing-base limitation. This limitation equals 80% of the net book value of Loans, less a hedging reserve (not exceeding \$1.0 million), and the amount of other debt secured by the collateral which secures the revolving secured line of credit facility. Borrowings under the revolving secured line of credit facility agreement are secured by a lien on most of our assets.

Warehouse Facilities

We have five Warehouse facilities with total borrowing capacity of \$975.0 million. Each of the facilities is with a different lender or group of lenders. Under each Warehouse facility, we can contribute Loans to our wholly-owned subsidiaries in return for cash and equity in each subsidiary. In turn, each subsidiary pledges the Loans as collateral to lenders to secure financing that will fund the cash portion of the purchase price of the Loans. The financing provided to each subsidiary under the applicable facility is generally limited to the lesser of 80% of the net book value of the contributed Loans plus the restricted cash and cash equivalents pledged as collateral on such Loans or the facility limit.

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

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

Term ABS Financings

We have wholly-owned subsidiaries (the “Funding LLCs”) that have completed secured financing transactions with qualified institutional investors or lenders. In connection with these transactions, we contributed Loans on an arms-length basis to each Funding LLC for cash and the sole membership interest in that Funding LLC. In turn, each Funding LLC, other than that of Term ABS 2016-1, contributed the Loans to a respective trust that issued notes to qualified institutional investors. The Funding LLC for the Term ABS 2016-1 transaction pledged the Loans to lenders.

The Term ABS 2015-2, 2016-2, 2016-3, 2017-1, 2017-2, 2017-3, 2018-1, 2018-2 and 2018-3 transactions each consist of three classes of notes.

Each financing at the time of issuance has a specified revolving period during which we are likely to contribute additional Loans to each Funding LLC. Each Funding LLC (other than that of Term ABS 2016-1) will then contribute the Loans to its respective trust. At the end of the revolving period, the debt outstanding under each financing will begin to amortize.

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

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

The table below sets forth certain additional details regarding the outstanding Term ABS financings:
(Dollars in millions)

Term ABS Financings	Close Date	Net Book Value of Loans Contributed at Closing	24 month Revolving Period
Term ABS 2015-2	August 20, 2015	\$ 375.5	Through August 15, 2017
Term ABS 2016-1	February 26, 2016	481.4	Through February 15, 2018
Term ABS 2016-2	May 12, 2016	437.8	Through May 15, 2018
Term ABS 2016-3	October 27, 2016	437.8	Through October 15, 2018
Term ABS 2017-1	February 23, 2017	437.8	Through February 15, 2019
Term ABS 2017-2	June 29, 2017	563.2	Through June 17, 2019
Term ABS 2017-3	October 26, 2017	437.6	Through October 15, 2019
Term ABS 2018-1	February 22, 2018	625.1	Through February 17, 2020
Term ABS 2018-2	May 24, 2018	562.6	Through May 15, 2020
Term ABS 2018-3	August 23, 2018	500.1	Through August 17, 2020

Senior Notes

On March 30, 2015, we issued \$250.0 million aggregate principal amount of 7.375% senior notes due 2023 (the “2023 senior notes”). The 2023 senior notes were issued pursuant to an indenture, dated as of March 30, 2015, among the Company, as issuer, the Company’s subsidiaries Buyers Vehicle Protection Plan, Inc. and Vehicle Remarketing Services, Inc., as guarantors (collectively, the “Guarantors”), and U.S. Bank National Association, as trustee.

The 2023 senior notes mature on March 15, 2023 and bear interest at a rate of 7.375% per annum, computed on the basis of a 360-day year composed of twelve 30-day months and payable semi-annually on March 15 and September 15 of each year, beginning on September 15, 2015. The 2023 senior notes were issued at a price of 99.266% of their aggregate principal amount, resulting in gross proceeds of \$248.2 million, and a yield to maturity of 7.5% per annum. We used the net proceeds from the offering of the notes for general corporate purposes, including repayment of

outstanding borrowings under our revolving secured line of credit facility.

On January 22, 2014, we issued \$300.0 million aggregate principal amount of 6.125% senior notes due 2021 (the “2021 senior notes”). The 2021 senior notes were issued pursuant to an indenture, dated as of January 22, 2014, among the Company, the Guarantors, and U.S. Bank National Association, as trustee.

The 2021 senior notes mature on February 15, 2021 and bear interest at a rate of 6.125% per annum, computed on the basis of a 360-day year composed of twelve 30-day months and payable semi-annually on February 15 and August 15 of each year, beginning on August 15, 2014. We used the net proceeds from the 2021 senior notes, together with borrowings under our revolving credit facilities, to redeem in full the \$350.0 million aggregate principal amount of our 9.125% first priority senior secured notes due 2017 on February 21, 2014.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

Both the 2021 and the 2023 senior notes (the "senior notes") are guaranteed on a senior basis by the Guarantors, which are also guarantors of obligations under our revolving secured line of credit facility. Other existing and future subsidiaries of ours may become guarantors of the senior notes in the future. The indentures for the senior notes provide for a guarantor of the senior notes to be released from its obligations under its guarantee of the senior notes under specified circumstances.

Mortgage Note

On August 6, 2018, we entered into a \$12.0 million mortgage note with a commercial bank that is secured by a first mortgage lien on a building acquired by us and an assignment of all leases, rents, revenues and profits under all present and future leases of the building. As of September 30, 2018, there was \$12.0 million outstanding on this note. The note matures on August 6, 2023, and bears interest at LIBOR plus 150 basis points.

Debt Covenants

As of September 30, 2018, we were in compliance with our covenants under the revolving secured line of credit facility, including those that require the maintenance of certain financial ratios and other financial conditions. These covenants require a minimum ratio of (1) our net earnings, adjusted for specified items, before income taxes, depreciation, amortization and fixed charges to (2) our fixed charges. These covenants also limit the maximum ratio of our funded debt less unrestricted cash and cash equivalents to tangible net worth. Additionally, we must maintain consolidated net income of not less than \$1 for the two most recently ended fiscal quarters. Some of these covenants may indirectly limit the repurchase of common stock or payment of dividends on common stock.

Our Warehouse facilities and Term ABS financings also contain covenants that measure the performance of the contributed assets. As of September 30, 2018, we were in compliance with all such covenants. As of the end of the quarter, we were also in compliance with our covenants under the senior notes indentures.

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

11. DERIVATIVE AND HEDGING INSTRUMENTS

Interest Rate Caps. We utilize interest rate cap agreements to manage the interest rate risk on certain secured financings. The following tables provide the terms of our interest rate cap agreements that were in effect as of September 30, 2018 and December 31, 2017:

(Dollars in millions)

As of September 30, 2018

Facility Amount	Facility Name	Purpose	Start	End	Notional	Cap Interest Rate (1)
\$400.0	Warehouse Facility II	Cap Floating Rate	12/2017	12/2020	\$ 205.0	5.50 %
250.0	Warehouse Facility IV	Cap Floating Rate	04/2016	04/2019	43.8	5.50 %
		Cap Floating Rate	05/2017	04/2021	56.2	6.50 %
		Cap Floating Rate	05/2018	04/2021	150.0	6.50 %
					250.0	
100.0	Warehouse Facility V	Cap Floating Rate	08/2018	08/2023	75.0	6.50 %
190.8	Term ABS 2016-1	Cap Floating Rate	04/2016	02/2019	160.4	5.00 %
150.0	Warehouse Facility VII	Cap Floating Rate	12/2017	11/2021	150.0	5.50 %

(Dollars in millions)

As of December 31, 2017

Facility Amount	Facility Name	Purpose	Start	End	Notional	Cap Interest Rate (1)
\$400.0	Warehouse Facility II	Cap Floating Rate	12/2017	12/2020	\$ 205.0	5.50 %
100.0	Warehouse Facility IV	Cap Floating Rate	04/2016	04/2019	75.0	5.50 %
		Cap Floating Rate	05/2017	04/2021	25.0	6.50 %
					100.0	
100.0	Warehouse Facility V	Cap Floating Rate	06/2015	07/2018	75.0	5.50 %
385.0	Term ABS 2016-1	Cap Floating Rate	04/2016	02/2019	385.0	5.00 %
150.0	Warehouse Facility VII	Cap Floating Rate	12/2017	11/2021	150.0	5.50 %

(1)Rate excludes the spread over the LIBOR rate.

The interest rate caps have not been designated as hedging instruments. As of September 30, 2018 and December 31, 2017, the interest rate caps had a fair value of \$0.1 million and \$0.0 million, respectively, as the capped rates were significantly above market rates.

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

12. INCOME TAXES

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

	For the Three		For the Nine	
	Months	Months	Months	Months
	Ended	Ended	Ended	Ended
	September	September	September	September
	30,	30,	30,	30,
	2018	2017	2018	2017
U.S. federal statutory income tax rate	21.0%	35.0%	21.0%	35.0%
State income taxes	2.5 %	1.9 %	2.5 %	1.8 %
Excess tax benefits from stock-based compensation plans	— %	— %	— %	-0.5 %
Other	0.4 %	0.2 %	0.3 %	0.2 %
Effective income tax rate	23.9%	37.1%	23.8%	36.5%

The decrease in our effective income tax rate for the three and nine months ended September 30, 2018 is primarily due to the enactment of the 2017 Tax Act, which lowered our federal statutory income tax rate from 35% to 21%.

The differences between the U.S. federal statutory income tax rate and our effective income tax rate are primarily due to state income taxes and excess tax benefits from stock-based compensation plans. We receive a tax deduction upon the vesting of restricted stock and the conversion of restricted stock units to common stock based on the fair value of the shares. The amount that this tax deduction differs from the grant-date fair value that was recognized as stock-based compensation expense is referred to as an excess tax benefit or deficiency.

Valuation allowance

As a result of the enactment of the 2017 Tax Act, we established a valuation allowance related to the executive compensation provisions of the law that limit a public entity's ability to deduct compensation for covered employees in excess of \$1.0 million for years after December 31, 2017, regardless of the nature of those payments. In prior years, qualifying performance-based compensation was excluded from the \$1.0 million limitation. Qualifying performance-based compensation paid in 2018 or later under written binding contracts that were in effect on November 2, 2017 will remain excluded from the \$1.0 million limitation unless such contracts are subsequently materially modified. We have made a reasonable estimate of the loss of tax benefits related to stock-based compensation, in accordance with ASU 2018-05. As of September 30, 2018 and December 31, 2017, the valuation allowance was \$6.3 million and \$5.5 million, respectively. This estimate may be refined in future periods as further information becomes available.

Valuation of Loans receivable

The 2017 Tax Act revises the rules associated with the timing of the recognition of income for federal income tax purposes. The 2017 Tax Act requires an accrual method taxpayer to recognize income no later than the taxable year in which such income is recognized as revenue in the financial statements, if the taxpayer is subject to the all events test—a requirement that all the events have occurred that fix the right to receive income, and that the amount can be determined with reasonable accuracy. The Senate Finance Committee intended that the new financial statement conformity requirement not be construed as preventing the use of special methods of accounting provided elsewhere in the Internal Revenue Code. It is unclear if our income recognition method related to the valuation of loans receivable is an allowable exception under the 2017 Tax Act. As we were not able to determine a reasonable estimate

based on current guidance, we will continue to apply ASC Topic 740, Income Taxes, in accordance with ASU 2018-05 and based on the provisions of the tax laws that were in effect immediately prior to the 2017 Tax Act being enacted. This treatment may change in future periods as further information becomes available.

Table of ContentsNOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

13. NET INCOME PER SHARE

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

	For the Three Months Ended September 30, 2018		For the Nine Months Ended September 30, 2017	
Weighted average shares outstanding:				
Common shares	19,158,654	19,150,749	19,157,004	19,277,014
Vested restricted stock units	306,909	256,595	299,385	251,161
Basic number of weighted average shares outstanding	19,465,563	19,407,344	19,456,389	19,528,175
Dilutive effect of restricted stock and restricted stock units	8,415	8,201	15,808	19,499
Dilutive number of weighted average shares outstanding	19,473,978	19,415,545	19,472,197	19,547,674

For the three months ended September 30, 2018 and September 30, 2017, and for the nine months ended September 30, 2018, there were no shares of restricted stock or restricted stock units that would have been anti-dilutive. For the nine months ended September 30, 2017, there were 250 shares of restricted stock and restricted stock units that were not included in the computation of diluted net income per share because their inclusion would have been anti-dilutive.

14. STOCK REPURCHASES

There were no stock repurchases for the three months ended September 30, 2018 and 2017. The following table summarizes our stock repurchases for the nine months ended September 30, 2018 and 2017:

(Dollars in millions)	For the Nine Months Ended September 30,			
	2018		2017	
	Number of Shares Repurchased	Cost	Number of Shares Repurchased	Cost
Open Market (1)	—	\$—	588,580	\$119.1
Other (2)	6,185	2.0	21,680	4.4
Total	6,185	\$2.0	610,260	\$123.5

Represents repurchases under authorizations by the board of directors for the repurchase of shares by us from time to time in the open market or in privately negotiated transactions. On February 13, 2017, the board of directors (1) authorized the repurchase of up to one million shares of our common stock in addition to the board's prior authorizations. As of September 30, 2018, we had authorization to repurchase 776,208 shares of our common stock.

(2) Represents shares of common stock released to us by team members as payment of tax withholdings upon the vesting of restricted stock and restricted stock units and the conversion of restricted stock units to common stock.

15. STOCK-BASED COMPENSATION PLANS

Stock-based compensation expense consists of the following:

(In millions)	For the		For the	
	Three	Nine	Three	Nine
	Months	Months	Months	Months
	Ended	Ended	Ended	Ended
	September	September	September	September
	30,	30,	30,	30,
	2018	2017	2018	2017
Restricted stock	\$0.7	\$0.8	\$2.1	\$2.2
Restricted stock units	2.0	2.1	5.7	6.1
Total	\$2.7	\$2.9	\$7.8	\$8.3

39

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)
(UNAUDITED)

16. COMMITMENTS AND CONTINGENCIES

Litigation and Other Legal Matters

In the normal course of business and as a result of the consumer-oriented nature of the industry in which we operate, we and other industry participants are frequently subject to various consumer claims, litigation and regulatory investigations seeking damages, fines and statutory penalties. The claims allege, among other theories of liability, violations of state, federal and foreign truth-in-lending, credit availability, credit reporting, consumer protection, warranty, debt collection, insurance and other consumer-oriented laws and regulations, including claims seeking damages for alleged physical and mental harm relating to the repossession and sale of consumers' vehicles and other debt collection activities. As the assignee of Consumer Loans originated by Dealers, we may also be named as a co-defendant in lawsuits filed by consumers principally against Dealers. We may also have disputes and litigation with Dealers. The claims may allege, among other theories of liability, that we breached our Dealer servicing agreement. We may also have disputes and litigation with vendors and other third parties. The claims may allege, among other theories of liability, that we breached a license agreement or contract. The damages, fines and penalties that may be claimed by consumers, regulatory agencies, Dealers, vendors or other third parties in these types of matters can be substantial. The relief requested by plaintiffs varies but may include requests for compensatory, statutory and punitive damages and injunctive relief, and plaintiffs may seek treatment as purported class actions. The following matters include current actions to which we are a party and updates to matters that were disclosed in our Annual Report on Form 10-K for the year ended December 31, 2017.

On April 10, 2018, we were informed by the New York Department of Financial Services, Financial Frauds & Consumer Protection Division (“DFS”) that it believes that the Company may have violated the law relating to fair lending; may have misrepresented to consumers information related to GPS Starter Interrupt Devices; and may have provided inaccurate information in the course of a DFS supervisory examination. We are cooperating with the inquiry, including through the exchange of certain written correspondence. We cannot predict the eventual scope, duration or outcome at this time. As a result, we are unable to estimate the reasonably possible loss or range of reasonably possible loss arising from this inquiry.

On December 4, 2014, we received a civil investigative demand from the Office of the Attorney General of the Commonwealth of Massachusetts relating to the origination and collection of non-prime auto loans in Massachusetts. On November 20, 2017 we received a second civil investigation demand from the Office of the Attorney General of the Commonwealth of Massachusetts seeking updated information on its original civil investigation demand, additional information related to the Company's origination and collection of Consumer Loans, and information regarding securitization activities. We are cooperating with the inquiry and cannot predict the eventual scope, duration or outcome at this time. As a result, we are unable to estimate the reasonably possible loss or range of reasonably possible loss arising from this investigation.

On August 14, 2017, we received a subpoena from the Attorney General of the State of Mississippi, relating to the origination and collection of non-prime auto loans in the state of Mississippi. We are cooperating with the inquiry and cannot predict the eventual scope, duration or outcome at this time. As a result, we are unable to estimate the reasonably possible loss or range of reasonably possible loss arising from this investigation.

On June 14, 2017, we were informed that the Bureau of Consumer Financial Protection's Office of Fair Lending and Equal Opportunity is investigating whether the Company may have violated the Equal Credit Opportunity Act and Regulation B. We are cooperating with the inquiry and cannot predict the eventual scope, duration or outcome at this

time. As a result, we are unable to estimate the reasonably possible loss or range of reasonably possible loss arising from this inquiry.

On November 7, 2016, we received a civil investigative demand from the Federal Trade Commission seeking information on the Company's policies, practices and procedures in allowing car dealers to use GPS Starter Interrupters on consumer vehicles. We are cooperating with the inquiry and cannot predict the eventual scope, duration or outcome at this time. As a result, we are unable to estimate the reasonably possible loss or range of reasonably possible loss arising from this investigation.

On March 18, 2016, we received a subpoena from the Attorney General of the State of Maryland, relating to the Company's repossession and sale policies and procedures in the state of Maryland. We are cooperating with the inquiry and cannot predict the eventual scope, duration or outcome at this time. As a result, we are unable to estimate the reasonably possible loss or range of reasonably possible loss arising from this investigation.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (CONCLUDED)
(UNAUDITED)

On February 19, 2016, we received a First Amended Complaint filed by Westlake Services d/b/a Westlake Financial Service and Nowcom Corporation, alleging that the Company has attempted to monopolize the indirect financing profit sharing program market in violation of Section 2 of the Sherman Act and seeking, among other things, injunctive relief and unspecified money damages, which, if awarded, would likely be trebled pursuant to the Sherman Act. The case was filed in the United States District Court, Central District of California, Western Division. On April 6, 2016, the Court dismissed the claims brought by Nowcom Corporation. On January 5, 2018, the Court entered judgment in favor of the Company, dismissing the case with prejudice on the merits and ordering that the Company be awarded its costs of suit from Westlake Services, LLC. On February 2, 2018, Westlake Services, LLC filed a Notice of Appeal with the Court. On July 13, 2018, Westlake Services, LLC filed its appellate brief with the United States Court of Appeals for the Ninth Circuit. On September 14, 2018, we filed our response to Westlake Services, LLC's appellate brief. On October 19, 2018, Westlake Services, LLC filed its reply brief. We cannot predict the duration or outcome of this lawsuit at this time. As a result, we are unable to estimate the reasonably possible loss or range of reasonably possible loss arising from this lawsuit. The Company intends to vigorously defend itself in this matter.

On September 18, 2015, we received a subpoena from the Attorney General of the State of New York, Civil Rights Bureau relating to the Company's origination and collection of Consumer Loans in the state of New York. We have cooperated with the inquiry, but cannot predict the eventual scope, duration or outcome at this time. As a result, we are unable to estimate the reasonably possible loss or range of reasonably possible loss arising from this investigation.

On December 9, 2014, we received a civil investigative subpoena from the U.S. Department of Justice pursuant to the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 directing us to produce certain information relating to subprime automotive finance and related securitization activities. We have cooperated with the inquiry, but cannot predict the eventual scope, duration or outcome at this time. As a result, we are unable to estimate the reasonably possible loss or range of reasonably possible loss arising from this investigation.

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

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

The following discussion and analysis should be read in conjunction with the consolidated financial statements and related notes included in Item 8 - Financial Statements and Supplementary Data, of our 2017 Annual Report on Form 10-K, as well as Item 1 - Financial Statements, of this Form 10-Q, which is incorporated herein by reference.

Overview

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

For the three months ended September 30, 2018, consolidated net income was \$151.0 million, or \$7.75 per diluted share, compared to \$100.7 million, or \$5.19 per diluted share, for the same period in 2017. For the nine months ended September 30, 2018, consolidated net income was \$422.1 million, or \$21.68 per diluted share, compared to \$293.1

million, or \$14.99 per diluted share, for the same period in 2017. The increases in consolidated net income for the three and nine months ended September 30, 2018 were primarily due to an increase in the average balance of our Loan portfolio, an improvement in Consumer Loan performance and the enactment of the 2017 Tax Act, which decreased our effective income tax rate.

41

Table of Contents

Critical Success Factors

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

Consumer Loan Metrics

At the time a Consumer Loan is submitted to us for assignment, we forecast future expected cash flows from the Consumer Loan. Based on the amount and timing of these forecasts and expected expense levels, an advance or one-time purchase payment is made to the related Dealer at a price designed to maximize economic profit.

We use a statistical model to estimate the expected collection rate for each Consumer Loan at the time of assignment. We continue to evaluate the expected collection rate of each Consumer Loan subsequent to assignment. Our evaluation becomes more accurate as the Consumer Loans age, as we use actual performance data in our forecast. By comparing our current expected collection rate for each Consumer Loan with the rate we projected at the time of assignment, we are able to assess the accuracy of our initial forecast. The following table compares our forecast of Consumer Loan collection rates as of September 30, 2018 with the forecasts as of June 30, 2018, December 31, 2017 and at the time of assignment, segmented by year of assignment:

Consumer Loan Assignment Year	Forecasted Collection Percentage as of (1)				Current Forecast Variance from			
	September 30, 2018	June 30, 2018	December 31, 2017	Initial Forecast	June 30, 2018	December 31, 2017	Initial Forecast	
2009	79.5%	79.5%	79.5%	71.9%	0.0%	0.0%	7.6%	
2010	77.7%	77.7%	77.6%	73.6%	0.0%	0.1%	4.1%	
2011	74.7%	74.8%	74.7%	72.5%	-0.1%	0.0%	2.2%	
2012	73.8%	73.8%	73.8%	71.4%	0.0%	0.0%	2.4%	
2013	73.5%	73.5%	73.5%	72.0%	0.0%	0.0%	1.5%	
2014	71.7%	71.7%	71.7%	71.8%	0.0%	0.0%	-0.1%	
2015	65.4%	65.4%	65.5%	67.7%	0.0%	-0.1%	-2.3%	
2016	64.3%	64.4%	64.8%	65.4%	-0.1%	-0.5%	-1.1%	
2017	65.6%	65.6%	65.6%	64.0%	0.0%	0.0%	1.6%	
2018 (2)	64.8%	64.5%	—	63.6%	0.3%	—	1.2%	

Represents the total forecasted collections we expect to collect on the Consumer Loans as a percentage of the repayments that we were contractually owed on the Consumer Loans at the time of assignment. Contractual (1) repayments include both principal and interest. Forecasted collection rates are negatively impacted by canceled Consumer Loans as the contractual amount owed is not removed from the denominator for purposes of computing forecasted collection rates in the table.

The forecasted collection rate for 2018 Consumer Loans as of September 30, 2018 includes both Consumer Loans (2) that were in our portfolio as of June 30, 2018 and Consumer Loans assigned during the most recent quarter. The following table provides forecasted collection rates for each of these segments:

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

2018 Consumer Loan Assignment Period	Forecasted Collection Percentage as of			Current Forecast Variance from	
	September 30, 2018	June 30, 2018	Initial Forecast	June 30, 2018	Initial Forecast
January 1, 2018 through June 30, 2018	65.3%	64.5%	63.6 %	0.8%	1.7 %
July 1, 2018 through September 30, 2018	63.8%	—	63.5 %	—	0.3 %

Consumer Loans assigned in 2009 through 2013, 2017 and 2018 have yielded forecasted collection results materially better than our initial estimates, while Consumer Loans assigned in 2015 and 2016 have yielded forecasted collection results materially worse than our initial estimates. For Consumer Loans assigned in 2014, actual results have been close to our initial estimates. For the three months ended September 30, 2018, forecasted collection rates improved for Consumer Loans assigned in 2018 and were generally consistent with expectations at the start of the period for all other assignment years presented. For the nine months ended September 30, 2018, forecasted collection rates improved for Consumer Loans assigned in 2018, declined for Consumer Loans assigned in 2016 and were generally consistent with expectations at the start of the period for all other assignment years presented.

Table of Contents

The changes in forecasted collection rates for the three and nine months ended September 30, 2018 and 2017 impacted forecasted net cash flows (forecasted collections less forecasted Dealer Holdback payments) as follows:

(In millions)	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Increase (Decrease) in Forecasted Net Cash Flows				
Dealer Loans	\$(0.1)	\$(1.9)	\$3.5	\$(6.8)
Purchased Loans	17.2	7.4	31.0	29.2
Total Loans	\$17.1	\$5.5	\$34.5	\$22.4

The following table presents information on the average Consumer Loan assignment for each of the last 10 years:

Consumer Loan Assignment Year	Average		Initial Loan Term (in months)
	Consumer Loan (1)	Advance (2)	
2009	\$12,689	\$ 5,565	38
2010	14,480	6,473	41
2011	15,686	7,137	46
2012	15,468	7,165	47
2013	15,445	7,344	47
2014	15,692	7,492	47
2015	16,354	7,272	50
2016	18,218	7,976	53
2017	20,230	8,746	55
2018 (3)	22,063	9,580	57

(1) Represents the repayments that we were contractually owed on Consumer Loans at the time of assignment, which include both principal and interest.

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

The averages for 2018 Consumer Loans include both Consumer Loans that were in our portfolio as of June 30, 2018 and Consumer Loans assigned during the most recent quarter. The following table provides averages for each of these segments:

2018 Consumer Loan Assignment Period	Average		Initial Loan Term (in months)
	Consumer Loan	Advance	
January 1, 2018 through June 30, 2018	\$21,995	\$ 9,542	57
July 1, 2018 through September 30, 2018	22,225	9,669	57

Table of Contents

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

The following table presents forecasted Consumer Loan collection rates, advance rates, the spread (the forecasted collection rate less the advance rate), and the percentage of the forecasted collections that had been realized as of September 30, 2018. All amounts, unless otherwise noted, are presented as a percentage of the initial balance of the Consumer Loan (principal + interest). The table includes both Dealer Loans and Purchased Loans.

Consumer Loan Assignment Year	As of September 30, 2018			
	Forecasted Collection %	Advance % (1)	Spread %	% of Forecast Realized (2)
2009	79.5%	43.9 %	35.6%	99.9 %
2010	77.7%	44.7 %	33.0%	99.6 %
2011	74.7%	45.5 %	29.2%	99.2 %
2012	73.8%	46.3 %	27.5%	98.7 %
2013	73.5%	47.6 %	25.9%	97.8 %
2014	71.7%	47.7 %	24.0%	94.5 %
2015	65.4%	44.5 %	20.9%	84.3 %
2016	64.3%	43.8 %	20.5%	65.7 %
2017	65.6%	43.2 %	22.4%	39.4 %
2018 (3)	64.8%	43.4 %	21.4%	11.4 %

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

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

(3) The forecasted collection rate, advance rate and spread for 2018 Consumer Loans as of September 30, 2018 include both Consumer Loans that were in our portfolio as of June 30, 2018 and Consumer Loans assigned during the most recent quarter. The following table provides forecasted collection rates, advance rates and spreads for each of these segments:

2018 Consumer Loan Assignment Period	As of September 30, 2018		
	Forecasted Collection %	Advance %	Spread %
January 1, 2018 through June 30, 2018	65.3%	43.4 %	21.9%
July 1, 2018 through September 30, 2018	63.8%	43.5 %	20.3%

The risk of a material change in our forecasted collection rate declines as the Consumer Loans age. For 2014 and prior Consumer Loan assignments, the risk of a material forecast variance is modest, as we have currently realized in excess of 90% of the expected collections. Conversely, the forecasted collection rates for more recent Consumer Loan assignments are less certain as a significant portion of our forecast has not been realized.

The spread between the forecasted collection rate and the advance rate has ranged from 20.5% to 35.6% over the last 10 years. The spread was at the high end of this range in 2009 and 2010, when the competitive environment was unusually favorable, and much lower during other years (2015 through 2018) when competition was more intense. The decrease in the spread from 2017 to 2018 was the result of a change in the mix of Consumer Loan assignments received during 2018, including an increase in Purchased Loans as a percentage of total unit volume, and the performance of 2017 Consumer Loans, which has exceeded our initial estimates by a greater margin than those assigned to us in 2018.

The decrease in the spread from the first six months of 2018 to the third quarter of 2018 was primarily the result of the performance of Consumer Loans assigned to us during the first six months of 2018, which has exceeded our initial estimates by a greater margin than those assigned to us during the third quarter of 2018.

Table of Contents

The following table compares our forecast of Consumer Loan collection rates as of September 30, 2018 with the forecasts at the time of assignment, for Dealer Loans and Purchased Loans separately:

Consumer Loan Assignment Year	Dealer Loans			Purchased Loans		
	Forecasted			Forecasted		
	Collection			Collection		
	Percentage as of			Percentage as of		
	(1)			(1)		
	September	Initial	Variance	September	Initial	Variance
	30,	Forecast		30,	Forecast	
	2018			2018		
2009	79.3%	72.1 %	7.2 %	80.8%	70.5 %	10.3 %
2010	77.6%	73.6 %	4.0 %	78.7%	73.1 %	5.6 %
2011	74.6%	72.4 %	2.2 %	76.3%	72.7 %	3.6 %
2012	73.7%	71.3 %	2.4 %	75.9%	71.4 %	4.5 %
2013	73.4%	72.1 %	1.3 %	74.3%	71.6 %	2.7 %
2014	71.6%	71.9 %	-0.3 %	72.6%	70.9 %	1.7 %
2015	64.6%	67.5 %	-2.9 %	69.5%	68.5 %	1.0 %
2016	63.4%	65.1 %	-1.7 %	66.9%	66.5 %	0.4 %
2017	64.9%	63.8 %	1.1 %	67.2%	64.6 %	2.6 %
2018	64.6%	63.6 %	1.0 %	65.4%	63.5 %	1.9 %

(1) The forecasted collection rates presented for Dealer Loans and Purchased Loans reflect the Consumer Loan classification at the time of assignment.

The following table presents forecasted Consumer Loan collection rates, advance rates, and the spread (the forecasted collection rate less the advance rate) as of September 30, 2018 for Dealer Loans and Purchased Loans separately. All amounts are presented as a percentage of the initial balance of the Consumer Loan (principal + interest).

Consumer Loan Assignment Year	Dealer Loans			Purchased Loans		
	Forecasted	Advance	Spread	Forecasted	Advance	Spread
	Collection	(1)	(2)	Collection	(1)	(2)
	% (1)	%	%	% (1)	%	%
2009	79.3%	43.4 %	35.9%	80.8%	46.0 %	34.8%
2010	77.6%	44.4 %	33.2%	78.7%	47.3 %	31.4%
2011	74.6%	45.1 %	29.5%	76.3%	49.3 %	27.0%
2012	73.7%	46.0 %	27.7%	75.9%	50.0 %	25.9%
2013	73.4%	47.2 %	26.2%	74.3%	51.5 %	22.8%
2014	71.6%	47.2 %	24.4%	72.6%	51.8 %	20.8%
2015	64.6%	43.4 %	21.2%	69.5%	50.2 %	19.3%
2016	63.4%	42.1 %	21.3%	66.9%	48.6 %	18.3%
2017	64.9%	42.1 %	22.8%	67.2%	45.8 %	21.4%
2018	64.6%	42.6 %	22.0%	65.4%	45.2 %	20.2%

(1) The forecasted collection rates and advance rates presented for Dealer Loans and Purchased Loans reflect the Consumer Loan classification at the time of assignment.

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

included.

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

The spread on Dealer Loans decreased from 22.8% in 2017 to 22.0% in 2018 primarily as a result of a change in the mix of Consumer Loan assignments.

The spread on Purchased Loans decreased from 21.4% in 2017 to 20.2% in 2018 primarily as a result of the performance of the 2017 Consumer Loans, which has exceeded our initial estimates by a greater margin than those assigned to us in 2018, and a change in the mix of Consumer Loan assignments.

45

Table of Contents

Access to Capital

Our strategy for accessing capital on acceptable terms needed to maintain and grow the business is to: (1) maintain consistent financial performance; (2) maintain modest financial leverage; and (3) maintain multiple funding sources. Our funded debt to equity ratio was 2.0 to 1 as of September 30, 2018. We currently utilize the following primary forms of debt financing: (1) a revolving secured line of credit; (2) Warehouse facilities; (3) Term ABS financings; and (4) senior notes.

Consumer Loan Volume

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

Three Months Ended	Year over Year Percent Change			
	Unit Volume		Dollar Volume	
	(1)			
March 31, 2017	-6.6 %	6.4 %		
June 30, 2017	1.0 %	7.1 %		
September 30, 2017	-4.7 %	-0.5 %		
December 31, 2017	10.8 %	26.2 %		
March 31, 2018	18.5 %	32.9 %		
June 30, 2018	19.8 %	34.7 %		
September 30, 2018	9.4 %	20.3 %		

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

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

Unit and dollar volumes grew 9.4% and 20.3%, respectively, during the third quarter of 2018 as the number of active Dealers grew 12.2% while average unit volume per active Dealer declined 2.9%. Dollar volume grew faster than unit volume during the third quarter of 2018 due to an increase in the average advance paid per unit. This increase was the result of an increase in the average size of the Consumer Loans assigned primarily due to increases in the average initial loan term and average vehicle selling price and an increase in purchased loans as a percentage of total unit volume.

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

	For the Three Months Ended September 30,			For the Nine Months Ended September 30,		
	2018	2017	% Change	2018	2017	% Change
Consumer Loan unit volume	86,005	78,589	9.4 %	290,976	250,715	16.1 %

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

Active Dealers (1)	8,684	7,737	12.2	%	11,390	10,484	8.6	%
Average volume per active Dealer	9.9	10.2	-2.9	%	25.5	23.9	6.7	%
Consumer Loan unit volume from Dealers active both periods	64,914	65,483	-0.9	%	240,914	221,000	9.0	%
Dealers active both periods	5,256	5,256	—		7,323	7,323	—	
Average volume per Dealer active both periods	12.4	12.5	-0.9	%	32.9	30.2	9.0	%
Consumer Loan unit volume from Dealers not active both periods	21,091	13,106	60.9	%	50,062	29,715	68.5	%
Dealers not active both periods	3,428	2,481	38.2	%	4,067	3,161	28.7	%
Average volume per Dealer not active both periods	6.2	5.3	17.0	%	12.3	9.4	30.9	%

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

Table of Contents

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

	For the Three Months Ended September 30,			For the Nine Months Ended September 30,		
	2018	2017	% Change	2018	2017	% Change
Consumer Loan unit volume from new active Dealers	3,785	4,063	-6.8 %	30,477	29,409	3.6 %
New active Dealers (1)	936	946	-1.1 %	3,005	2,821	6.5 %
Average volume per new active Dealer	4.0	4.3	-7.0 %	10.1	10.4	-2.9 %
Attrition (2)	-16.7 %	-23.7 %		-11.9 %	-12.7 %	

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

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

The following table shows the percentage of Consumer Loans assigned to us as Dealer Loans and Purchased Loans for each of the last seven quarters:

Three Months Ended	Unit Volume		Dollar Volume (1)	
	Dealer Loans	Purchased Loans	Dealer Loans	Purchased Loans
March 31, 2017	73.3%	26.7 %	67.8%	32.2 %
June 30, 2017	72.3%	27.7 %	67.9%	32.1 %
September 30, 2017	71.9%	28.1 %	68.6%	31.4 %
December 31, 2017	72.5%	27.5 %	69.7%	30.3 %
March 31, 2018	70.1%	29.9 %	67.4%	32.6 %
June 30, 2018	69.7%	30.3 %	66.8%	33.2 %
September 30, 2018	69.5%	30.5 %	67.0%	33.0 %

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

As of September 30, 2018 and December 31, 2017, the net Dealer Loans receivable balance was 65.8% and 68.2%, respectively, of the total net Loans receivable balance.

Table of Contents

Results of Operations

Three Months Ended September 30, 2018 Compared to Three Months Ended September 30, 2017

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

(Dollars in millions, except per share data)	For the Three Months Ended			
	September 30,		Change	% Change
	2018	2017		
Revenue:				
Finance charges	\$ 303.0	\$ 259.4	\$ 43.6	16.8 %
Premiums earned	12.2	10.3	1.9	18.4 %
Other income	16.8	14.2	2.6	18.3 %
Total revenue	332.0	283.9	48.1	16.9 %
Costs and expenses:				
Salaries and wages (1)	41.1	33.7	7.4	22.0 %
General and administrative (1)	14.1	14.2	(0.1)	-0.7 %
Sales and marketing (1)	16.3	14.2	2.1	14.8 %
Provision for credit losses	14.0	25.7	(11.7)	-45.5 %
Interest	41.1	30.5	10.6	34.8 %
Provision for claims	7.0	5.5	1.5	27.3 %
Total costs and expenses	133.6	123.8	9.8	7.9 %
Income before provision for income taxes	198.4	160.1	38.3	23.9 %
Provision for income taxes	47.4	59.4	(12.0)	-20.2 %
Net income	\$ 151.0	\$ 100.7	\$ 50.3	50.0 %
Net income per share:				
Basic	\$ 7.76	\$ 5.19	\$ 2.57	49.5 %
Diluted	\$ 7.75	\$ 5.19	\$ 2.56	49.3 %
Weighted average shares outstanding:				
Basic	19,465,568	19,407,344	58,219	0.3 %
Diluted	19,473,978	19,415,545	58,433	0.3 %
(1) Operating expenses	\$ 71.5	\$ 62.1	\$ 9.4	15.1 %

Table of Contents

Finance Charges. The increase of \$43.6 million, or 16.8%, was primarily the result of an increase in the average net Loans receivable balance partially offset by a decrease in the average yield on our Loan portfolio, as follows:

(Dollars in millions)	For the Three Months Ended		
	September 30,		
	2018	2017	Change
Average net Loans receivable balance	\$5,458.3	\$4,365.8	\$1,092.5
Average yield on our Loan portfolio	22.2	% 23.8	% -1.6 %

The following table summarizes the impact each component had on the overall increase in finance charges for the three months ended September 30, 2018:

(In millions)	Year over Year Change For the Three Months Ended September 30, 2018
Impact on finance charges:	
Due to an increase in the average net Loans receivable balance	\$ 64.9
Due to a decrease in the average yield	(21.3)
Total increase in finance charges	\$ 43.6

The increase in the average net Loans receivable balance was primarily due to the dollar volume of new Consumer Loan assignments exceeding the principal collected on Loans receivable. The average yield on our Loan portfolio for the three months ended September 30, 2018 decreased as compared to the same period in 2017 due to lower yields on more recent Consumer Loan assignments.

Other income. The increase of \$2.6 million, or 18.3%, was primarily due to an increase in ancillary product profit sharing income primarily due to growth in our Loan portfolio.

Operating Expenses. The increase of \$9.4 million, or 15.1%, was primarily due to the following:

• An increase in salaries and wages expense of \$7.4 million, or 22.0%, as a result of the following:

• An increase of \$4.7 million in cash-based incentive compensation expense primarily due to an improvement in Company performance measures.

Excluding the change in cash-based incentive compensation expense, salaries and wages expense increased \$2.7 million, primarily related to increases of \$2.1 million for our support function and \$0.6 million for our servicing function primarily as a result of an increase in the number of team members.

• An increase in sales and marketing expense of \$2.1 million, or 14.8%, primarily due to an increase in the size of our sales force and an increase in sales commissions related to growth in Consumer Loan assignment volume.

Provision for Credit Losses. Under GAAP, when the present value of forecasted future cash flows declines relative to our expectations at the time of assignment, a provision for credit losses is recorded immediately as a current period expense and a corresponding allowance for credit losses is established. For purposes of calculating the required allowance, Dealer Loans are grouped by Dealer and Purchased Loans are grouped by month of purchase. As a result, regardless of the overall performance of the portfolio of Consumer Loans, a provision can be required if any

individual Loan pool performs worse than expected. Conversely, a previously recorded provision can be reversed if any previously impaired individual Loan pool experiences an improvement in performance.

During the three months ended September 30, 2018, overall Consumer Loan performance was consistent with our expectations at the start of the period. However, the performance of certain Loan pools declined from our expectations during the period, resulting in a provision for credit losses of \$14.0 million for the three months ended September 30, 2018, of which \$12.4 million related to Dealer Loans and \$1.6 million related to Purchased Loans. During the three months ended September 30, 2017, overall Consumer Loan performance was generally consistent with our expectations at the start of the period. However, the performance of certain Loan pools declined from our expectations during the period, resulting in a provision for credit losses of \$25.7 million for the three months ended September 30, 2017, of which \$20.2 million related to Dealer Loans and \$5.5 million related to Purchased Loans.

Table of Contents

Interest. The increase of \$10.6 million, or 34.8%, was primarily due to increases in the average outstanding debt principal balance. The following table shows interest expense, the average outstanding debt balance, and the average cost of debt for the three months ended September 30, 2018 and 2017:

(Dollars in millions)	For the Three Months Ended September 30,		
	2018	2017	Change
Interest expense	\$41.1	\$30.5	\$10.6
Average outstanding debt principal balance (1)	3,807.6	2,997.8	809.8
Average cost of debt	4.3 %	4.1 %	0.2 %

(1) Includes the unamortized debt discount and excludes deferred debt issuance costs.

The average outstanding debt principal balance increased primarily due to borrowings used to fund the growth in our Loan portfolio.

Provision for Income Taxes. For the three months ended September 30, 2018, the effective income tax rate decreased to 23.9% from 37.1% for the three months ended September 30, 2017. The decrease was primarily due to the enactment of the 2017 Tax Act, which decreased our federal statutory income tax rate from 35% to 21%.

Table of Contents

Nine Months Ended September 30, 2018 Compared to Nine Months Ended September 30, 2017

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

(Dollars in millions, except per share data)	For the Nine Months Ended			
	September 30,		Change	% Change
	2018	2017		
Revenue:				
Finance charges	\$863.0	\$ 749.2	113.8	15.2 %
Premiums earned	34.2	30.9	3.3	10.7 %
Other income	45.8	42.6	3.2	7.5 %
Total revenue	943.0	822.7	120.3	14.6 %
Costs and expenses:				
Salaries and wages (1)	123.3	101.9	21.4	21.0 %
General and administrative (1)	41.3	42.1	(0.8)	-1.9 %
Sales and marketing (1)	51.3	43.7	7.6	17.4 %
Provision for credit losses	39.2	68.0	(28.8)	-42.4 %
Interest	114.3	88.0	26.3	29.9 %
Provision for claims	19.5	17.6	1.9	10.8 %
Total costs and expenses	388.9	361.3	27.6	7.6 %
Income before provision for income taxes	554.1	461.4	92.7	20.1 %
Provision for income taxes	132.0	168.3	(36.3)	-21.6 %
Net income	\$422.1	\$ 293.1	\$129.0	44.0 %
Net income per share:				
Basic	\$21.69	\$ 15.01	\$6.68	44.5 %
Diluted	\$21.68	\$ 14.99	\$6.69	44.6 %
Weighted average shares outstanding:				
Basic	19,456,389	19,528,175	(71,786)	-0.4 %
Diluted	19,472,197	19,547,674	(75,477)	-0.4 %
(1) Operating expenses	\$215.9	\$ 187.7	28.2	15.0 %

Table of Contents

Finance Charges. The increase of \$113.8 million, or 15.2%, was primarily the result of an increase in the average net Loans receivable balance partially offset by a decrease in the average yield on our Loan portfolio, as follows:

(Dollars in millions)	For the Nine Months Ended		
	September 30,		
	2018	2017	Change
Average net Loans receivable balance	\$5,147.4	\$4,184.3	\$963.1
Average yield on our Loan portfolio	22.4	% 23.9	% -1.5 %

The following table summarizes the impact each component had on the overall increase in finance charges for the nine months ended September 30, 2018:

(In millions)	Year over Year Change For the Nine Months Ended September 30, 2018
Impact on finance charges:	
Due to an increase in the average net Loans receivable balance	\$ 172.4
Due to a decrease in the average yield	(58.6)
Total increase in finance charges	\$ 113.8

The increase in the average net Loans receivable balance was primarily due to the dollar volume of new Consumer Loan assignments exceeding the principal collected on Loans receivable. The average yield on our Loan portfolio for the nine months ended September 30, 2018 decreased as compared to the same period in 2017 due to lower yields on more recent Consumer Loan assignments.

Operating Expenses. The increase of \$28.2 million, or 15.0%, was primarily due to the following:

• An increase in salaries and wages expense of \$21.4 million, or 21.0%, as a result of the following:

• An increase of \$11.5 million in cash-based incentive compensation expense primarily due to an improvement in Company performance measures.

Excluding the change in cash-based incentive compensation expense, salaries and wages expense increased \$9.9 million, primarily related to increases of \$6.3 million for our support function and \$2.8 million for our servicing function primarily as a result of an increase in the number of team members.

• An increase in sales and marketing expense of \$7.6 million, or 17.4%, primarily due to an increase in sales commissions related to growth in Consumer Loan assignment volume and an increase in the size of our sales force.

Provision for Credit Losses. During the nine months ended September 30, 2018, overall Consumer Loan performance was consistent with our expectations at the start of the period. However, the performance of certain Loan pools declined from our expectations during the period, resulting in a provision for credit losses of \$39.2 million for the nine months ended September 30, 2018, of which \$34.3 million related to Dealer Loans and \$4.9 million related to Purchased Loans. During the nine months ended September 30, 2017, overall Consumer Loan performance was generally consistent with our expectations at the start of the period. However, the performance of certain Loan pools declined from our expectations during the period, resulting in a provision for credit losses of \$68.0 million for the nine months ended September 30, 2017, of which \$55.6 million related to Dealer Loans and \$12.4 million related to

Purchased Loans.

52

Table of Contents

Interest. The increase of \$26.3 million, or 29.9%, was primarily due to an increase in the average outstanding debt principal balance. The following table shows interest expense, the average outstanding debt balance, and the average cost of debt for the nine months ended September 30, 2018 and 2017:

(Dollars in millions)	For the Nine Months Ended		
	September 30,		
	2018	2017	Change
Interest expense	\$114.3	\$88.0	\$26.3
Average outstanding debt principal balance (1)	3,581.0	2,890.8	690.2
Average cost of debt	4.3	% 4.1	% 0.2 %

(1) Includes the unamortized debt discount and excludes deferred debt issuance costs.

The average outstanding debt principal balance increased primarily due to borrowings used to fund the growth in our Loan portfolio.

Provision for Income Taxes. For the nine months ended September 30, 2018, the effective income tax rate decreased to 23.8% from 36.5% for the nine months ended September 30, 2017. The decrease was primarily due to the enactment of the 2017 Tax Act, which decreased our federal statutory income tax rate from 35% to 21%.

Liquidity and Capital Resources

We need capital to maintain and grow our business. Our primary sources of capital are cash flows from operating activities, collections of Consumer Loans and borrowings under: (1) a revolving secured line of credit; (2) Warehouse facilities; (3) Term ABS financings; and (4) senior notes. There are various restrictive covenants to which we are subject under each financing arrangement and we were in compliance with those covenants as of September 30, 2018. For information regarding these financings and the covenants included in the related documents, see Note 10 to the consolidated financial statements contained in Item 1 of this Form 10-Q, which is incorporated herein by reference.

On February 22, 2018, we completed a \$500.0 million Term ABS financing, which was used to repay outstanding indebtedness. The financing has an expected annualized cost of approximately 3.6% (including the initial purchasers' fees and other costs), and it will revolve for 24 months, after which it will amortize based upon the cash flows on the contributed Loans.

On May 10, 2018, we added a new lender to Warehouse Facility IV and increased the financing amount on the facility from \$100.0 million to \$250.0 million. There were no other material changes to the terms of the facility.

On May 24, 2018, we completed a \$450.0 million Term ABS financing, which was used to repay outstanding indebtedness. The financing has an expected annualized cost of approximately 4.0% (including the initial purchasers' fees and other costs), and it will revolve for 24 months, after which it will amortize based upon the cash flows on the contributed Loans.

On June 27, 2018, we extended the maturity of our revolving secured line of credit facility from June 22, 2020 to June 22, 2021. There were no other material changes to the terms of the facility. As previously disclosed, the amount of the facility will decrease to \$315.0 million on June 22, 2019.

On August 6, 2018, we entered into a \$12.0 million mortgage note with a commercial bank that is secured by a first mortgage lien on a building acquired by us and an assignment of all leases, rents, revenues and profits under all present and future leases of the building. As of September 30, 2018, there was \$12.0 million outstanding on this note. The note matures on August 6, 2023, and bears interest at LIBOR plus 150 basis points.

On August 15, 2018, we extended the date on which our \$100.0 million Warehouse Facility V will cease to revolve from August 18, 2019 to August 17, 2021. The maturity of the facility was also extended from August 18, 2021 to August 17, 2023. The interest rate on borrowings under the facility has decreased from LIBOR plus 225 basis points to LIBOR plus 190 basis points. There were no other material changes to the terms of the facility.

On August 23, 2018, we completed a \$398.3 million Term ABS financing, which was used to repay outstanding indebtedness. The financing has an expected annualized cost of approximately 4.0% (including the initial purchasers' fees and other costs), and it will revolve for 24 months, after which it will amortize based upon the cash flows on the contributed Loans.

Table of Contents

Cash and cash equivalents as of September 30, 2018 and December 31, 2017 was \$195.7 million and \$8.2 million, respectively. As of September 30, 2018 and December 31, 2017, we had \$1,325.0 million and \$1,161.1 million in unused and available lines of credit, respectively. Our total balance sheet indebtedness increased \$806.1 million to \$3,876.9 million as of September 30, 2018 from \$3,070.8 million as of December 31, 2017 primarily due to the growth in new Consumer Loan assignments.

Contractual Obligations

A summary of our scheduled principal debt maturities as of September 30, 2018 is as follows:
(In millions)

Year	Scheduled Principal Debt Maturities (1)
Remainder of 2018	\$ 223.3
2019	1,006.3
2020	1,335.0
2021	1,077.1
2022	0.7
Over five years	259.3
Total	\$ 3,901.7

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

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

Critical Accounting Estimates

Our consolidated financial statements are prepared in accordance with GAAP. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. On an ongoing basis, we review our accounting policies, assumptions, estimates and judgments to ensure that our financial statements are presented fairly and in accordance with GAAP. Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2017 discusses several critical accounting estimates, which we believe involve a high degree of judgment and complexity. There have been no material changes to the estimates and assumptions associated with these accounting estimates from those discussed in our Annual Report on Form 10-K for the year ended December 31, 2017.

Off-Balance Sheet Arrangements

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

Forward-Looking Statements

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

Table of Contents

We claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995 for all of our forward-looking statements. These forward-looking statements represent our outlook only as of the date of this report. While we believe that our forward-looking statements are reasonable, actual results could differ materially since the statements are based on our current expectations, which are subject to risks and uncertainties. Factors that might cause such a difference include, but are not limited to, the factors set forth in Item 1A of our Form 10-K for the year ended December 31, 2017, other risk factors discussed herein or listed from time to time in our reports filed with the SEC and the following:

• Our inability to accurately forecast and estimate the amount and timing of future collections could have a material adverse effect on results of operations.

• We may be unable to execute our business strategy due to current economic conditions.

• We may be unable to continue to access or renew funding sources and obtain capital needed to maintain and grow our business.

• The terms of our debt limit how we conduct our business.

• A violation of the terms of our Term ABS facilities or Warehouse facilities could have a material adverse impact on our operations.

The conditions of the U.S. and international capital markets may adversely affect lenders with which we have relationships, causing us to incur additional costs and reducing our sources of liquidity, which may adversely affect our financial position, liquidity and results of operations.

• Our substantial debt could negatively impact our business, prevent us from satisfying our debt obligations and adversely affect our financial condition.

• Due to competition from traditional financing sources and non-traditional lenders, we may not be able to compete successfully.

• We may not be able to generate sufficient cash flows to service our outstanding debt and fund operations and may be forced to take other actions to satisfy our obligations under such debt.

• Interest rate fluctuations may adversely affect our borrowing costs, profitability and liquidity.

• Reduction in our credit rating could increase the cost of our funding from, and restrict our access to, the capital markets and adversely affect our liquidity, financial condition and results of operations.

• We may incur substantially more debt and other liabilities. This could exacerbate further the risks associated with our current debt levels.

• The regulation to which we are or may become subject could result in a material adverse effect on our business.

Adverse changes in economic conditions, the automobile or finance industries, or the non-prime consumer market could adversely affect our financial position, liquidity and results of operations, the ability of key vendors that we depend on to supply us with services, and our ability to enter into future financing transactions.

Litigation we are involved in from time to time may adversely affect our financial condition, results of operations and cash flows.

- Changes in tax laws and the resolution of uncertain income tax matters could have a material adverse effect on our results of operations and cash flows from operations.

Our dependence on technology could have a material adverse effect on our business.

Our use of electronic contracts could impact our ability to perfect our ownership or security interest in Consumer Loans.

Table of Contents

Reliance on third parties to administer our ancillary product offerings could adversely affect our business and financial results.

We are dependent on our senior management and the loss of any of these individuals or an inability to hire additional team members could adversely affect our ability to operate profitably.

Our reputation is a key asset to our business, and our business may be affected by how we are perceived in the marketplace.

The concentration of our Dealers in several states could adversely affect us.

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

A small number of our shareholders have the ability to significantly influence matters requiring shareholder approval and such shareholders have interests which may conflict with the interests of our other security holders.

Reliance on our outsourced business functions could adversely affect our business.

Our ability to hire and retain foreign information technology personnel could be hindered by immigration restrictions.

Natural disasters, acts of war, terrorist attacks and threats or the escalation of military activity in response to these attacks or otherwise may negatively affect our business, financial condition and results of operations.

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

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Refer to our Annual Report on Form 10-K for the year ended December 31, 2017 for a complete discussion of our market risk. There have been no material changes to the market risk information included in our 2017 Annual Report on Form 10-K.

ITEM 4. CONTROLS AND PROCEDURES.

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

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

56

Table of Contents

PART II. - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In the normal course of business and as a result of the consumer-oriented nature of the industry in which we operate, we and other industry participants are frequently subject to various consumer claims, litigation and regulatory investigations seeking damages, fines and statutory penalties. The claims allege, among other theories of liability, violations of state, federal and foreign truth-in-lending, credit availability, credit reporting, consumer protection, warranty, debt collection, insurance and other consumer-oriented laws and regulations, including claims seeking damages for alleged physical and mental harm relating to the repossession and sale of consumers' vehicles and other debt collection activities. As the assignee of Consumer Loans originated by Dealers, we may also be named as a co-defendant in lawsuits filed by consumers principally against Dealers. We may also have disputes and litigation with Dealers. The claims may allege, among other theories of liability, that we breached our Dealer servicing agreement. We may also have disputes and litigation with vendors and other third parties. The claims may allege, among other theories of liability, that we breached a license agreement or contract. The damages, fines and penalties that may be claimed by consumers, regulatory agencies, Dealers, vendors or other third parties in these types of matters can be substantial. The relief requested by plaintiffs varies but may include requests for compensatory, statutory and punitive damages and injunctive relief, and plaintiffs may seek treatment as purported class actions. An adverse ultimate disposition in any action to which we are a party or otherwise subject could have a material adverse impact on our financial position, liquidity and results of operations.

For a description of significant litigation to which we are a party, see Note 16 to the consolidated financial statements contained in Part I - Item 1 of this Form 10-Q, which is incorporated herein by reference.

Table of Contents

ITEM 6. EXHIBITS

Exhibit

No.	Description
<u>4.95</u>	Third Amendment to Loan and Security Agreement, dated as of August 15, 2018 among the Company, CAC Warehouse Funding LLC V, Fifth Third Bank and Systems & Services Technologies, Inc. (incorporated by reference to Exhibit 4.95 to the Company's Current Report on Form 8-K filed August 17, 2018).
<u>4.96</u>	Indenture dated as of August 23, 2018, between Credit Acceptance Auto Loan Trust 2018-3 and Wells Fargo Bank, National Association (incorporated by reference to Exhibit 4.96 to the Company's Current Report on Form 8-K filed August 29, 2018).
<u>4.97</u>	Sale and Servicing Agreement dated as of August 23, 2018 among the Company, Credit Acceptance Auto Loan Trust 2018-3, Credit Acceptance Funding LLC 2018-3, and Wells Fargo Bank, National Association (incorporated by reference to Exhibit 4.97 to the Company's Current Report on Form 8-K filed August 29, 2018).
<u>4.98</u>	Backup Servicing Agreement dated as of August 23, 2018, among the Company, Credit Acceptance Funding LLC 2018-3, Credit Acceptance Auto Loan Trust 2018-3, and Wells Fargo Bank, National Association (incorporated by reference to Exhibit 4.98 to the Company's Current Report on Form 8-K filed August 29, 2018).
<u>4.99</u>	Amended and Restated Trust Agreement dated as of August 23, 2018, among Credit Acceptance Funding LLC 2018-3, each of the members of the Board of Trustees of the Trust and U.S. Bank Trust National Association (incorporated by reference to Exhibit 4.99 to the Company's Current Report on Form 8-K filed August 29, 2018).
<u>4.100</u>	Sale and Contribution Agreement dated as of August 23, 2018, between the Company and Credit Acceptance Funding LLC 2018-3 (incorporated by reference to Exhibit 4.100 to the Company's Current Report on Form 8-K filed August 29, 2018).
<u>4.101</u>	Amended and Restated Intercreditor Agreement dated August 23, 2018, among the Company, CAC Warehouse Funding Corporation II, CAC Warehouse Funding LLC IV, CAC Warehouse Funding LLC V, CAC Warehouse Funding LLC VI, CAC Warehouse Funding LLC VII, Credit Acceptance Funding LLC 2018-3, Credit Acceptance Funding LLC 2018-2, Credit Acceptance Funding LLC 2018-1, Credit Acceptance Funding LLC 2017-3, Credit Acceptance Funding LLC 2017-2, Credit Acceptance Funding LLC 2017-1, Credit Acceptance Funding LLC 2016-3, Credit Acceptance Funding LLC 2016-2, Credit Acceptance Funding LLC 2016-1, Credit Acceptance Funding LLC 2015-2, Credit Acceptance Auto Loan Trust 2018-3, Credit Acceptance Auto Loan Trust 2018-2, Credit Acceptance Auto Loan Trust 2018-1, Credit Acceptance Auto Loan Trust 2017-3, Credit Acceptance Auto Loan Trust 2017-2, Credit Acceptance Auto Loan Trust 2017-1, Credit Acceptance Auto Loan Trust 2016-3, Credit Acceptance Auto Loan Trust 2016-2, Credit Acceptance Auto Loan Trust 2015-2, Wells Fargo Bank, National Association, as agent and as indenture trustee, Fifth Third Bank, as agent, Bank of Montreal, as agent, Flagstar Bank, FSB, as agent and Comerica Bank, as agent (incorporated by reference to Exhibit 4.101 to the Company's Current Report on Form 8-K filed August 29, 2018).
<u>31.1</u>	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
<u>31.2</u>	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
<u>32.1</u>	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
<u>32.2</u>	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101(INS)	XBRL Instance Document.

Edgar Filing: CREDIT ACCEPTANCE CORP - Form 10-Q

- 101(SCH) XBRL Taxonomy Extension Schema Document.
- 101(CAL) XBRL Taxonomy Extension Calculation Linkbase Document.
- 101(DEF) XBRL Taxonomy Extension Definition Linkbase Document.
- 101(LAB) XBRL Taxonomy Extension Label Linkbase Document.
- 101(PRE) XBRL Taxonomy Extension Presentation Linkbase Document.

Unless otherwise noted, the Company's commission file number for all exhibits incorporated by reference herein is 000-20202.

58

Table of Contents

SIGNATURES

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

CREDIT ACCEPTANCE CORPORATION
(Registrant)

By: /s/ Kenneth S. Booth
Kenneth S. Booth
Chief Financial Officer
(Principal Financial Officer and Principal Accounting Officer)
Date: October 29, 2018