AMERICAS CARMART INC
Form 10-Q
September 06, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended July 31, 2016

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: 0-14939

AMERICA'S CAR-MART, INC.

(Exact name of registrant as specified in its charter)

Texas	**63-0851141**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

802 Southeast Plaza Ave., Suite 200, Bentonville, Arkansas 72712

(Address of principal executive offices) (zip code)

(479) 464-9944

(Registrant's telephone number, including area 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 and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

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

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

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

Title of Each Class	Outstanding at September 5, 2016
Common stock, par value $.01 per share	7,836,197

Part I. FINANCIAL INFORMATION

Item 1. Financial Statements America's Car-Mart, Inc.

Condensed Consolidated Balance Sheets

(Unaudited)

(Dollars in thousands except share and per share amounts)

	July 31, 2016	April 30, 2016
Assets:		
Cash and cash equivalents	$371	$602
Accrued interest on finance receivables	2,157	1,716
Finance receivables, net	352,548	334,793
Inventory	33,824	29,879
Prepaid expenses and other assets	3,264	3,302
Income taxes receivable, net	-	894
Goodwill	355	355
Property and equipment, net	34,182	34,755
Total Assets	$426,701	$406,296
Liabilities, mezzanine equity and equity:		
Liabilities:		
Accounts payable	$14,468	$12,313
Deferred payment protection plan revenue	18,116	17,304
Deferred service contract revenue	10,369	10,035
Accrued liabilities	15,256	11,245
Income taxes payable, net	1,940	-
Deferred income tax liabilities, net	19,223	18,280
Revolving credit facilities and notes payable	117,534	107,902
Total liabilities	196,906	177,079
Commitments and contingencies (Note J)		
Mezzanine equity:		
Mandatorily redeemable preferred stock	400	400
Equity:		
Preferred stock, par value $.01 per share, 1,000,000 shares authorized; none issued or outstanding	-	-
	127	127

Common stock, par value $.01 per share, 50,000,000 shares authorized; 12,731,779 and 12,726,560 issued at July 31, 2016 and April 30, 2016, respectively, of which 7,805,947 and 8,073,820 were outstanding at July 31, 2016 and April 30, 2016, respectively		
Additional paid-in capital	65,415	64,771
Retained earnings	312,453	305,354
Less: Treasury stock, at cost, 4,925,832 and 4,652,740 shares at July 31, 2016 and April 30, 2016, respectively	(148,700)	(141,535)
Total stockholders' equity	229,295	228,717
Non-controlling interest	100	100
Total equity	229,395	228,817
Total Liabilities, Mezzanine Equity and Equity	$426,701	$406,296

The accompanying notes are an integral part of these condensed consolidated financial statements.

Condensed Consolidated Statements of Operations America's Car-Mart, Inc.

(Unaudited)

(Dollars in thousands except share and per share amounts)

	Three Months Ended July 31, 2016	2015
Revenues:		
Sales	$129,684	$127,595
Interest and other income	16,156	15,095
Total revenue	145,840	142,690
Costs and expenses:		
Cost of sales	75,513	75,087
Selling, general and administrative	23,168	23,125
Provision for credit losses	33,381	35,345
Interest expense	944	760
Depreciation and amortization	1,096	1,010
Loss on disposal of property and equipment	400	-
Total costs and expenses	134,502	135,327
Income before taxes	11,338	7,363
Provision for income taxes	4,229	2,747
Net income	$7,109	$4,616
Less: Dividends on mandatorily redeemable preferred stock	(10)	(10)
Net income attributable to common stockholders	$7,099	$4,606
Earnings per share:		
Basic	$0.89	$0.54
Diluted	$0.87	$0.52
Weighted average number of shares used in calculation:		
Basic	7,948,925	8,513,440
Diluted	8,185,077	8,909,597

The accompanying notes are an integral part of these condensed consolidated financial statements.

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Condensed Consolidated Statements of Cash Flows America's Car-Mart, Inc.

(Unaudited)

(In thousands)

	Three Months Ended July 31,	
Operating Activities:	2016	2015
Net income	$7,109	$4,616
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Provision for credit losses	33,381	35,345
Losses on claims for payment protection plan	3,107	3,155
Depreciation and amortization	1,096	1,010
Amortization of debt issuance costs	70	48
Loss on disposal of property and equipment	400	-
Stock based compensation	532	665
Deferred income taxes	943	469
Excess tax benefit from share based compensation	-	(191)
Change in operating assets and liabilities:		
Finance receivable originations	(120,848)	(117,341)
Finance receivable collections	58,036	58,943
Accrued interest on finance receivables	(441)	192
Inventory	4,624	7,690
Prepaid expenses and other assets	38	305
Accounts payable and accrued liabilities	3,678	1,890
Deferred payment protection plan revenue	812	540
Deferred service contract revenue	334	514
Income taxes, net	2,834	2,192
Net cash (used in) provided by operating activities	(4,295)	42
Investing Activities:		
Purchase of property and equipment	(523)	(1,398)
Net cash used in investing activities	(523)	(1,398)
Financing Activities:		
Exercise of stock options	77	245
Excess tax benefit from share based compensation	-	191
Issuance of common stock	35	69
Purchase of common stock	(7,165)	(2,311)
Dividend payments	(10)	(10)
Change in cash overdrafts	2,088	392
Payments on note payable	(26)	-
Proceeds from revolving credit facilities	94,410	87,857
Payments on revolving credit facilities	(84,822)	(85,132)
Net cash provided by financing activities	4,587	1,301

Decrease in cash and cash equivalents	(231)	(55)
Cash and cash equivalents, beginning of period	602	790
Cash and cash equivalents, end of period	$371	$735

The accompanying notes are an integral part of these condensed consolidated financial statements.

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Notes to Consolidated Financial Statements (Unaudited) **America's Car-Mart, Inc.**

A – Organization and Business

America's Car-Mart, Inc., a Texas corporation (the "Company"), is one of the largest publicly held automotive retailers in the United States focused exclusively on the "Integrated Auto Sales and Finance" segment of the used car market. References to the Company typically include the Company's consolidated subsidiaries. The Company's operations are principally conducted through its two operating subsidiaries, America's Car Mart, Inc., an Arkansas corporation ("Car-Mart of Arkansas"), and Colonial Auto Finance, Inc., an Arkansas corporation ("Colonial"). The Company primarily sells older model used vehicles and provides financing for substantially all of its customers. Many of the Company's customers have limited financial resources and would not qualify for conventional financing as a result of limited credit histories or past credit problems. As of July 31, 2016, the Company operated 143 dealerships located primarily in small cities throughout the South-Central United States.

B – Summary of Significant Accounting Policies

General

The accompanying condensed consolidated balance sheet as of April 30, 2016, which has been derived from audited financial statements, and the unaudited interim condensed financial statements as of July 31, 2016 and 2015, have been prepared in accordance with generally accepted accounting principles for interim financial information and in accordance 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 accounting principles generally accepted in the United States of America 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. Operating results for the three months ended July 31, 2016 are not necessarily indicative of the results that may be expected for the year ending April 30, 2017. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's annual report on Form 10-K for the year ended April 30, 2016.

Principles of Consolidation

The consolidated financial statements include the accounts of America's Car-Mart, Inc. and its subsidiaries. All intercompany accounts and transactions have been eliminated.

Segment Information

Each dealership is an operating segment with its results regularly reviewed by the Company's chief operating decision maker in an effort to make decisions about resources to be allocated to the segment and to assess its performance. Individual dealerships meet the aggregation criteria for reporting purposes under the current accounting guidance. The Company operates in the Integrated Auto Sales and Finance segment of the used car market, also referred to as the Integrated Auto Sales and Finance industry. In this industry, the nature of the sale and the financing of the transaction, financing processes, the type of customer and the methods used to distribute the Company's products and services, including the actual servicing of the contracts as well as the regulatory environment in which the Company operates, all have similar characteristics. Each of our individual dealerships is similar in nature and only engages in the selling and financing of used vehicles. All individual dealerships have similar operating characteristics. As such, individual dealerships have been aggregated into one reportable segment.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions 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 period. Actual results could differ from those estimates. Significant estimates include, but are not limited to, the Company's allowance for credit losses.

Concentration of Risk

The Company provides financing in connection with the sale of substantially all of its vehicles. These sales are made primarily to customers residing in Alabama, Arkansas, Georgia, Kentucky, Mississippi, Missouri, Oklahoma, Tennessee, and Texas, with approximately 31% of revenues resulting from sales to Arkansas customers.

Periodically, the Company maintains cash in financial institutions in excess of the amounts insured by the federal government. The Company's revolving credit facilities mature in October 2017. The Company expects that these credit facilities will be renewed or refinanced on or before the scheduled maturity dates.

Restrictions on Distributions/Dividends

The Company's revolving credit facilities generally restrict distributions by the Company to its shareholders. The distribution limitations under the Credit Facilities allow the Company to repurchase the Company's stock so long as: either (a) the aggregate amount of such repurchases does not exceed $40 million beginning October 8, 2014 and the sum of borrowing bases combined minus the principal balances of all revolver loans after giving effect to such repurchases is equal to or greater than 30% of the sum of the borrowing bases, or (b) the aggregate amount of such repurchases does not exceed 75% of the consolidated net income of the Company measured on a trailing twelve month basis; provided that immediately before and after giving effect to the stock repurchases, at least 12.5% of the aggregate funds committed under the credit facilities remain available. Thus, the Company is limited in its ability to pay dividends or make other distributions to its shareholders without the consent of the Company's lenders.

Cash Equivalents

The Company considers all highly liquid debt instruments purchased with original maturities of three months or less to be cash equivalents.

Finance Receivables, Repossessions and Charge-offs and Allowance for Credit Losses

The Company originates installment sale contracts from the sale of used vehicles at its dealerships. These installment sale contracts typically carry an interest rate of 15% using the simple effective interest method including any deferred fees. In May 2016, the Company increased its retail installment sales contract interest rate from 15.0% to 16.5% in response to continued high levels of credit losses. Contract origination costs are not significant. The installment sale contracts are not pre-computed contracts whereby borrowers are obligated to pay back principal plus the full amount of interest that will accrue over the entire term of the contract. Finance receivables are collateralized by vehicles sold and consist of contractually scheduled payments from installment contracts net of unearned finance charges and an allowance for credit losses. Unearned finance charges represent the balance of interest receivable to be earned over the entire term of the related installment contract, less the earned amount ($2.2 million at July 31, 2016 and $1.7 million April 30, 2016 on the Condensed Consolidated Balance Sheets), and as such, have been reflected as a reduction to the gross contract amount in arriving at the principal balance in finance receivables. An account is considered delinquent when the customer is one day or more behind on their contractual payments. While the Company does not formally place contracts on nonaccrual status, the immaterial amount of interest that may accrue after an account becomes delinquent up until the point of resolution via repossession or write-off, is reserved for against the accrued interest on the Condensed Consolidated Balance Sheets. Delinquent contracts are addressed and either made current by the customer, which is the case in most situations, or the vehicle is repossessed or written off if the collateral cannot be recovered quickly. Customer payments are set to match their payday with approximately 73% of payments due on either a weekly or bi-weekly basis. The frequency of the payment due dates combined with the declining value of collateral lead to prompt resolutions on problem accounts. At July 31, 2016, 4.4% of the Company's finance receivable balances were 30 days or more past due compared to 3.8% at July 31, 2015.

Substantially all of the Company's automobile contracts involve contracts made to individuals with impaired or limited credit histories or higher debt-to-income ratios than permitted by traditional lenders. Contracts made with buyers who are restricted in their ability to obtain financing from traditional lenders generally entail a higher risk of delinquency, default and repossession, and higher losses than contracts made with buyers with better credit.

The Company strives to keep its delinquency percentages low, and not to repossess vehicles. Accounts two days late are sent a notice in the mail. Accounts three days late are contacted by telephone. Notes from each telephone contact are electronically maintained in the Company's computer system. The Company attempts to resolve payment delinquencies amicably prior to repossessing a vehicle. If a customer becomes severely delinquent in his or her payments, and management determines that timely collection of future payments is not probable, the Company will take steps to repossess the vehicle. Periodically, the Company enters into contract modifications with its customers to extend or modify the payment terms. The Company only enters into a contract modification or extension if it believes such action will increase the amount of monies the Company will ultimately realize on the customer's account and will increase the likelihood of the customer being able to pay off the vehicle contract. At the time of modification, the Company expects to collect amounts due including accrued interest at the contractual interest rate for the period of delay. No other concessions beyond the extension of additional time are granted to customers at the time of modifications. Modifications are minor and are made for payday changes, minor vehicle repairs and other reasons. For those vehicles that are repossessed, the majority are returned or surrendered by the customer on a voluntary basis. Other repossessions are performed by Company personnel or third party repossession agents. Depending on the condition of a repossessed vehicle, it is either resold on a retail basis through a Company dealership, or sold for cash on a wholesale basis primarily through physical or online auctions.

The Company takes steps to repossess a vehicle when the customer becomes delinquent in his or her payments and management determines that timely collection of future payments is not probable. Accounts are charged-off after the expiration of a statutory notice period for repossessed accounts, or when management determines that the timely collection of future payments is not probable for accounts where the Company has been unable to repossess the vehicle. For accounts with respect to which the vehicle was repossessed, the fair value of the repossessed vehicle is charged as a reduction of the gross finance receivables balance charged-off. For the quarter ended July 31, 2016, on average, accounts were approximately 60 days past due at the time of charge-off. For previously charged-off accounts that are subsequently recovered, the amount of such recovery is credited to the allowance for credit losses.

The Company maintains an allowance for credit losses on an aggregate basis at a level it considers sufficient to cover estimated losses inherent in the portfolio at the balance sheet date in the collection of its finance receivables currently outstanding. At July 31, 2016, the weighted average total contract term was 31.7 months with 23.3 months remaining. The reserve amount in the allowance for credit losses at July 31, 2016, $108.0 million, was 25% of the principal balance in finance receivables of $460.6 million, less unearned payment protection plan revenue of $18.1 million and unearned service contract revenue of $10.4 million.

The estimated reserve amount is the Company’s anticipated future net charge-offs for losses incurred through the balance sheet date. The allowance takes into account historical credit loss experience (both timing and severity of losses), with consideration given to recent credit loss trends and changes in contract characteristics (i.e., average amount financed, months outstanding at loss date, term and age of portfolio), delinquency levels, collateral values, economic conditions and underwriting and collection practices. The allowance for credit losses is reviewed at least quarterly by management with any changes reflected in current operations. The calculation of the allowance for credit losses uses the following primary factors:

- The number of units repossessed or charged-off as a percentage of total units financed over specific historical periods of time from one year to five years.
- The average net repossession and charge-off loss per unit during the last eighteen months segregated by the number of months since the contract origination date and adjusted for the expected future average net charge-off loss per unit. About 50% of the charge-offs that will ultimately occur in the portfolio are expected to occur within 10-11 months following the balance sheet date. The average age of an account at charge-off date for the eighteen-month period ended July 31, 2016 was 11.8 months.
- The timing of repossession and charge-off losses relative to the date of sale (i.e., how long it takes for a repossession or charge-off to occur) for repossessions and charge-offs occurring during the last eighteen months.

A point estimate is produced by this analysis which is then supplemented by any positive or negative subjective factors to arrive at an overall reserve amount that management considers to be a reasonable estimate of losses inherent in the portfolio at the balance sheet date that will be realized via actual charge-offs in the future. Although it is at least reasonably possible that events or circumstances could occur in the future that are not presently foreseen which could cause actual credit losses to be materially different from the recorded allowance for credit losses, the Company believes that it has given appropriate consideration to all relevant factors and has made reasonable assumptions in determining the allowance for credit losses. While challenging economic conditions can negatively impact credit losses, the effectiveness of the execution of internal policies and procedures within the collections area and the competitive environment on the funding side have historically had a more significant effect on collection results than macro-economic issues.

In most states, the Company offers retail customers who finance their vehicle the option of purchasing a payment protection plan product as an add-on to the installment sale contract. This product contractually obligates the Company to cancel the remaining principal outstanding for any contract where the retail customer has totaled the vehicle, as defined by the contract, or the vehicle has been stolen. The Company periodically evaluates anticipated losses to ensure that if anticipated losses exceed deferred payment protection plan revenues, an additional liability is recorded for such difference. No such liability was required at July 31, 2016 or 2015.

Inventory

Inventory consists of used vehicles and is valued at the lower of cost or market on a specific identification basis. Vehicle reconditioning costs are capitalized as a component of inventory. Repossessed vehicles and trade-in vehicles are recorded at fair value, which approximates wholesale value. The cost of used vehicles sold is determined using the specific identification method.

Goodwill

Goodwill reflects the excess of purchase price over the fair value of specifically identified net assets purchased. Goodwill and intangible assets deemed to have indefinite lives are not amortized but are subject to annual impairment tests at the Company's year-end. The impairment tests are based on the comparison of the fair value of the reporting unit to the carrying value of such unit. If the fair value of the reporting unit falls below its carrying value, the Company performs the second step of the two-step goodwill impairment process to determine the amount, if any, that the goodwill is impaired. The second step involves determining the fair value of the identifiable assets and liabilities and the implied goodwill. The implied goodwill is compared to the carrying value of the goodwill to determine the impairment, if any. There was no impairment of goodwill during fiscal 2016, and to date, there has been no impairment during fiscal 2017.

Property and Equipment

Property and equipment are stated at cost. Expenditures for additions, remodels and improvements are capitalized. Costs of repairs and maintenance are expensed as incurred. Leasehold improvements are amortized over the shorter of the estimated life of the improvement or the lease period. The lease period includes the primary lease term plus any extensions that are reasonably assured. Depreciation is computed principally using the straight-line method, generally over the following estimated useful lives:

Furniture, fixtures and equipment (years)	3	to	7
Leasehold improvements (years)	5	to	15
Buildings and improvements (years)	18	to	39

Property and equipment are reviewed for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying values of the impaired assets exceed the fair value of such assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

Cash Overdraft

As checks are presented for payment from the Company's primary disbursement bank account, monies are automatically drawn against cash collections for the day and, if necessary, are drawn against one of the revolving credit facilities. Any cash overdraft balance principally represents outstanding checks that as of the balance sheet date had not yet been presented for payment, net of any deposits in transit. Any cash overdraft balance is reflected in accrued liabilities on the Company’s Condensed Consolidated Balance Sheets.

Deferred Sales Tax

Deferred sales tax represents a sales tax liability of the Company for vehicles sold on an installment basis in the states of Alabama and Texas. Under Alabama and Texas law, for vehicles sold on an installment basis the related sales tax is due as the payments are collected from the customer, rather than at the time of sale. Deferred sales tax liabilities are reflected in accrued liabilities on the Company’s Condensed Consolidated Balance Sheets.

Income Taxes

Income taxes are accounted for under the liability method. Under this method, deferred income tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities, and are measured using the enacted tax rates expected to apply in the years in which these differences are expected to be recovered or settled. The quarterly provision for income taxes is determined using an estimated annual effective tax rate, which is based on expected annual taxable income, statutory tax rates and the Company’s best estimate of nontaxable and nondeductible items of income and expense.

Occasionally, the Company is audited by taxing authorities. These audits could result in proposed assessments of additional taxes. The Company believes that its tax positions comply in all material respects with applicable tax law. However, tax law is subject to interpretation, and interpretations by taxing authorities could be different from those of the Company, which could result in the imposition of additional taxes.

The Company recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the more-likely-than-not threshold, the amount recognized in the financial statements is the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority. The Company applies this methodology to all tax positions for which the statute of limitations remains open.

The Company is subject to income taxes in the U.S. federal jurisdiction and various state jurisdictions. Tax regulations within each jurisdiction are subject to the interpretation of the related tax laws and regulations and require significant judgment to apply. With few exceptions, the Company is no longer subject to U.S. federal, state and local income tax examinations by tax authorities for the years before fiscal 2013.

The Company’s policy is to recognize accrued interest related to unrecognized tax benefits in interest expense and penalties in operating expenses. The Company had no accrued penalties or interest as of July 31, 2016 or April 30, 2016.

Revenue Recognition

Revenues are generated principally from the sale of used vehicles, which in most cases includes a service contract and a payment protection plan product, interest income and late fees earned on finance receivables. Revenues are net of taxes collected from customers and remitted to government agencies. Cost of vehicle sales include costs incurred by the Company to prepare the vehicle for sale including license and title costs, gasoline, transport services and repairs.

Revenues from the sale of used vehicles are recognized when financing, if applicable, has been approved, the sales contract is signed, and the customer has taken possession of the vehicle. Revenues from the sale of vehicles sold at wholesale are recognized at the time the proceeds are received. Revenues from the sale of service contracts are initially deferred and then recognized ratably over the expected duration of the product. Service contract revenues are included in sales and the related expenses are included in cost of sales. Payment protection plan revenues are initially deferred and then recognized to income using the “Rule of 78’s” interest method over the life of the contract so that revenues are recognized in proportion to the amount of cancellation protection provided. Payment protection plan revenues recognized are included in sales and related losses are included in cost of sales as incurred. Interest income is recognized on all active finance receivable accounts using the simple effective interest method. Active accounts include all accounts except those that have been paid-off or charged-off.

Sales consist of the following:

	Three Months Ended July 31,	
(In thousands)	2016	2015
Sales – used autos	$112,735	$110,647
Wholesales – third party	5,417	5,619
Service contract sales	6,761	6,812
Payment protection plan revenue	4,771	4,517
Total	$129,684	$127,595

At July 31, 2016 and 2015, finance receivables more than 90 days past due were approximately $1.7 million and $1.4 million, respectively. Late fee revenues totaled approximately $461,000 and $526,000 for the three months ended July 31, 2016 and 2015, respectively. Late fees are recognized when collected and are reflected in interest and other income on the Condensed Consolidated Statements of Operations.

Earnings per Share

Basic earnings per share are computed by dividing net income attributable to common stockholders by the average number of common shares outstanding during the period. Diluted earnings per share are computed by dividing net income attributable to common stockholders by the average number of common shares outstanding during the period plus dilutive common stock equivalents. The calculation of diluted earnings per share takes into consideration the potentially dilutive effect of common stock equivalents, such as outstanding stock options and non-vested restricted stock, which if exercised or converted into common stock would then share in the earnings of the Company. In computing diluted earnings per share, the Company utilizes the treasury stock method and anti-dilutive securities are excluded.

Stock-Based Compensation

The Company recognizes the cost of employee services received in exchange for awards of equity instruments, such as stock options and restricted stock, based on the fair value of those awards at the date of grant over the requisite service period. The Company uses the Black-Scholes option pricing model to determine the fair value of stock option awards. The Company may issue either new shares or treasury shares upon exercise of these awards. Stock-based compensation plans, related expenses and assumptions used in the Black-Scholes option pricing model are more fully described in Note I. If an award contains a performance condition, expense is recognized only for those shares for which it is considered reasonably probable as of the current period end that the performance condition will be met.

Treasury Stock

The Company purchased 273,092 shares of its common stock to be held as treasury stock for a total cost of $7.2 million during the first three months of fiscal 2017 and 46,000 shares for a total cost of $2.3 million during the first three months of fiscal 2016. Treasury stock may be used for issuances under the Company's stock-based compensation plans or for other general corporate purposes. During fiscal 2016, the Company established a reserve account of 10,000 shares of treasury stock to secure outstanding service contracts issued in Iowa in accordance with the regulatory requirements of that state.

Recent Accounting Pronouncements

Occasionally, new accounting pronouncements are issued by the Financial Accounting Standards Board ("FASB") or other standard setting bodies which the Company will adopt as of the specified effective date. Unless otherwise discussed, the Company believes the impact of recently issued standards which are not yet effective will not have a material impact on its consolidated financial statements upon adoption.

Revenue Recognition. In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers* (Topic 606), which supersedes existing revenue recognition guidance. The new guidance in 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. In August 2015, the FASB issued ASU 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, to provide entities with an additional year to implement ASU 2014-09. As a result, the guidance in ASU 2014-09 is effective for annual and interim reporting periods beginning after December 15, 2017, using one of two retrospective application methods. The Company is currently evaluating the potential effects of the adoption of this update on the consolidated financial statements.

Leases. In February 2016, the FASB issued ASU 2016-02, *Leases*. The new guidance requires that lessees recognize all leases, including operating leases, with a term greater than 12 months on-balance sheet and also requires disclosure of key information about leasing transactions. The guidance in ASU 2016-02 is effective for annual and interim reporting periods beginning after December 15, 2018. The Company is currently evaluating the potential effects of the adoption of this guidance on the consolidated financial statements.

Stock Compensation. In March 2016, the FASB issued ASU 2016-09, *Improvements to Employee Share-Based Payment Accounting*, which aims to simplify aspects of accounting for share-based payment transactions, including: presenting the excess tax benefit or deficit from the exercise or vesting of share-based payments in the income statement, a revision to the criteria for classifying an award as equity or liability, an option to recognize gross stock compensation expense with actual forfeitures recognized as they occur, and certain classifications on the statement of cash flows. In addition, the new guidance eliminates the excess tax benefit from the assumed proceeds calculation under the treasury stock method for purposes of calculating diluted shares. ASU 2016-09 is effective for annual and interim reporting periods beginning after December 15, 2016. Certain provisions of ASU 2016-09 are required to be adopted prospectively, notably the requirement to recognize the excess tax benefit or deficit in the income statement, while other provisions require modified retrospective application or in some cases full retrospective application. The Company is currently evaluating the potential effects of the adoption of this guidance on the consolidated financial statements.

Credit Losses. In June 2016, the FASB issued ASU 2016-13, *Financial Instruments — Credit Losses* (Topic 326). ASU 2016-13 requires financial assets such as loans to be presented net of an allowance for credit losses that reduces the cost basis to the amount expected to be collected over the estimated life. Expected credit losses will be measured based on historical experience and current conditions, as well as forecasts of future conditions that affect the collectability of the reported amount. ASU 2016-13 is effective for annual and interim reporting periods beginning after December 15, 2019, using a modified retrospective approach. The Company is currently evaluating the potential effects of the adoption of this guidance on the consolidated financial statements.

Reclassifications

The Company has made reclassifications to certain amounts in the accompanying Condensed Consolidated Balance Sheet as of April 30, 2016. The reclassifications did not have an impact on net income or earnings per share.

C – Finance Receivables, Net

The Company originates installment sale contracts from the sale of used vehicles at its dealerships. These installment sale contracts carry an interest rate of 15% or 16.5% per annum (based on the Company's contract interest rate as of the contract origination date), are collateralized by the vehicle sold and typically provide for payments over periods ranging from 18 to 42 months. The weighted average interest rate for the portfolio was approximately 15.16% at July 31, 2016. The Company's finance receivables are defined as one segment and one class of loans in sub-prime consumer automobile contracts. The level of risks inherent in the Company's financing receivables is managed as one homogeneous pool.