

CONSUMER PORTFOLIO SERVICES INC  
Form S-3/A  
July 20, 2006

As filed with the Securities and Exchange Commission on July 20, 2006

Registration No. 333-135357

**U.S. SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**Amendment No. 1 to Form S-3 Registration Statement  
Under the Securities Act of 1933**

**Consumer Portfolio Services, Inc.**

(Exact name of registrant as specified in its charter)

**California**

(State or other  
jurisdiction of  
incorporation or  
organization)

**33-0459135**

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

**16355 Laguna Canyon Road, Irvine, California 92618, Telephone: (949) 753-6800**

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

Charles E. Bradley, Jr.  
**Consumer Portfolio Services, Inc.**  
16355 Laguna Canyon Road  
Irvine, California 92618

Telephone: (949) 753-6800, Fax: (949) 753-6897

(Name, address, including zip code, and telephone number, including area code, of agents for service)

*Copies to:*

Patrick C. Sargent, Esq.  
Mark W. Harris, Esq.  
**Andrews Kurth LLP**  
1717 Main Street, Suite  
3700  
Dallas, Texas 75201  
Telephone: (214) 659-4400

Thomas J. Poletti, Esq.  
Shoshannah D. Katz, Esq.  
**Kirkpatrick & Lockhart Nicholson Graham  
LLP**  
10100 Santa Monica Boulevard, 7th Floor  
Los Angeles, California 90067  
Telephone: (310) 552-5000

Mitchell S. Cohen, Esq.  
**Irell & Manella LLP**  
1800 Avenue of the Stars  
Suite 900  
Los Angeles, California 90067  
Telephone: (310) 277-1010

Fax: (214) 659-4401

Fax: (310) 552-5001

Fax: (310) 203-7199

Approximate date of commencement of proposed sale to the public: **As soon as practicable after this Registration Statement becomes effective.**

If the only securities being registered on this form are being offered pursuant to dividend or interest reinvestment plans, please check the following box. "

If any of the securities being registered on this form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box. "

If this form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. "

If this form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. "

If this form is a registration statement pursuant to General Instruction I.D. or a post-effective amendment thereto that shall become effective upon filing with the Commission pursuant to Rule 462(e) under the Securities Act, check the following box. "

If this form is a post-effective amendment to a registration statement filed pursuant to General Instruction I.D. filed to register additional securities or additional classes of securities pursuant to Rule 413(b) under the Securities Act, check the following box. "

#### CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to Be Registered	Amount to Be Registered	Proposed Maximum Offering Price Per Unit (1)	Proposed Maximum Aggregate Offering Price (1)	Amount of Registration Fee (2)
Common stock, no par value	4,600,000 shares (3)	\$ 6.73	\$ 30,958,000	\$ 3,313
Common stock, no par value (1)	575,000 shares	\$ 6.77	\$ 3,892,750	\$ 417

Estimated solely for the purpose of calculating the registration fee pursuant to Rule 457(c) under the Securities Act, based on the average of high and low prices reported for the registrant's Common stock by the Nasdaq National Market on June 20, 2006 (\$6.73 per share) and on July 14, 2006 (\$6.77 per share).

(2)

A filing fee of \$3,313 was paid with the filing of the Registrant's Registration Statement on June 27, 2006. An additional filing fee in the amount of \$417 is being paid with the filing of this Amendment.

(3)

Includes 1,000 shares of common stock underlying a warrant to be exercised immediately prior to the consummation of this offering.

---

**The information in this prospectus is not complete and may be changed. We have filed a registration statement with the Securities and Exchange Commission relating to the common stock. The common stock may not be sold nor may offers to buy be accepted prior to the time the registration statement becomes effective. This prospectus is not an offer to sell the common stock, and neither we nor the selling shareholders are soliciting offers to buy these securities in any jurisdiction where the offer or sale is not permitted.**

**SUBJECT TO COMPLETION DATED JULY 20, 2006**

**PRELIMINARY PROSPECTUS**

**Consumer Portfolio Services, Inc.**

4,500,000 Shares

Common Stock

We are a specialty finance company engaged in sub-prime automobile finance, which includes the purchase and servicing of automobile contracts originated primarily by franchised automobile dealers. We indirectly provide financing to vehicle purchasers who typically have limited or impaired credit histories that restrict their ability to obtain financing through traditional lending sources.

We are offering 500,000 shares of our common stock and two selling shareholders, Levine Leichtman Capital Partners II, L.P. and Stanwich Financial Services Corp., are offering a total of 4,000,000 shares of our common stock. We will not receive any of the proceeds from the sale of shares of common stock by the selling shareholders. Levine Leichtman Capital Partners II, L.P., one of our principal shareholders, beneficially owned approximately 18.3% of our common stock as of June 30, 2006, and also holds \$40.0 million of our outstanding secured senior indebtedness. As of June 30, 2006, Stanwich Financial Services Corp. beneficially owned approximately 2.5% of our common stock.

Our common stock is traded on the Nasdaq National Market under the symbol CPSS. On July 18, 2006, the last reported sale price of our common stock on the Nasdaq National Market was \$7.00 per share.

**Investing in our common stock involves a high degree of risk.  
See Risk Factors beginning on page 8.**

	<b>Per Share</b>	<b>Total</b>
Public offering price	\$	\$
Underwriting discounts and commissions	\$	\$
Proceeds, before expenses, to us (1)	\$	\$
Proceeds, before expenses, to the selling shareholders (2)	\$	\$
(1)		

We estimate that we will incur approximately \$170,000 in offering expenses in connection with this offering.

(2)

We will pay all offering expenses related to the offering and sale of shares of our common stock in this offering by the selling shareholders (other than the underwriting discounts and commissions of the selling shareholders).

**Neither the Securities and Exchange Commission nor any state securities commission or regulatory authority has approved or disapproved of these securities or passed upon the accuracy or adequacy of this prospectus. Any representation to the contrary is a criminal offense.**

We and the selling shareholders have granted the underwriter a 30-day option to purchase up to an additional 675,000 shares of our common stock to cover over-allotments, if any, at the public offering price per share, less discounts and commissions.

The underwriter expects that the shares of our common stock will be ready for delivery to purchasers on or about , 2006.

**JMP Securities**

**The date of this prospectus is , 2006**

*You should rely only upon the information contained in, or incorporated into, this prospectus. We have not authorized any other person to provide you with different information. We have supplied all information contained or incorporated by reference relating to Consumer Portfolio Services, Inc. and our subsidiaries. Each selling shareholder has supplied certain information contained in this prospectus relating to that selling shareholder. If anyone provides you with different or inconsistent information, you should not rely on it. Neither we nor the selling shareholders are making an offer to sell our common stock in any jurisdiction where the offer or sale is not permitted. You should assume the information appearing in this document is accurate only as of the date on the front cover of this prospectus. Our business, financial condition, results of operations and prospects may have changed since that date.*

## TABLE OF CONTENTS

	<b>Page</b>
Prospectus Summary	
1	
Risk Factors	
8	
Forward-Looking Statements	
17	
Use of Proceeds	
17	
Price Range of Common Stock	
18	
Dividend Policy	
18	
Capitalization	
19	
Selected Consolidated Financial Data	
20	
Management's Discussion and Analysis of Financial Condition and Results of Operations	
22	
Our Company	
41	
Management	
50	
Certain Transactions	

52

Principal and Selling Shareholders

54

Description of Capital Stock

55

Selling Shareholders

56

Underwriting

58

Legal Matters

60

Experts

60

Where You Can Find More Information

60

Documents Incorporated by Reference

60

Index to Consolidated Financial Statements

F-1

Independent Registered Public Accounting Firm Reports

F-2

## PROSPECTUS SUMMARY

*This summary provides a brief overview of certain information found in greater detail elsewhere in this prospectus. It does not contain all the information that may be important to you in making a decision to purchase our common stock. We urge you to read the entire prospectus carefully, including Risk Factors and our consolidated financial statements and related notes, before deciding to invest in our common stock. For more complete information, you should carefully read this prospectus and the documents referred to in Where You Can Find More Information and Documents Incorporated by Reference. Unless we indicate otherwise, all information in this prospectus assumes the underwriter will not exercise its over-allotment option. Unless otherwise indicated, all references to we, us and similar terms mean Consumer Portfolio Services, Inc. and its subsidiaries.*

### **Our Company**

We are a specialty finance company engaged in purchasing and servicing new and used retail automobile contracts originated primarily by franchised automobile dealerships and, to a lesser extent, by select independent dealers of used automobiles in the United States. We serve as an alternative source of financing for dealers, facilitating sales to sub-prime customers, who have limited credit histories, low incomes or past credit problems and who otherwise might not be able to obtain financing from traditional lending sources. We do not currently lend money directly to consumers but, rather, purchase automobile contracts from dealers under several different financing programs. We are headquartered in Irvine, California and have three additional strategically located servicing branches in Virginia, Florida and Illinois.

We began our operations in October 1991. From our inception through March 31, 2006, we have purchased, in aggregate, approximately \$6.3 billion of automobile contracts from dealers. In addition, we obtained a total of approximately \$605.0 million of automobile contracts in three acquisitions in 2002, 2003 and 2004. We establish our relationships with dealers through our marketing representatives. As of March 31, 2006, we had 84 marketing representatives and we had active contract relationships with over 7,300 dealers in 47 states. Approximately 92% of these dealers are franchised new car dealers that sell both new and used cars and the remainder are independent used car dealers. For the year ended December 31, 2005, approximately 81% of the automobile contracts purchased under our programs consisted of financing for used cars and 19% consisted of financing for new cars.

We purchase automobile contracts with the intention of financing them on a long-term basis through securitizations. Depending on the structure of the securitization, the transaction may be treated as a sale of the contracts or as a secured financing for financial accounting purposes. Since the third quarter of 2003, we have structured our securitization transactions to be treated as secured financings for financial accounting purposes, which means the contracts and the asset-backed notes issued remain on our balance sheet, and the interest income from the contracts and the related financing costs of the asset-backed notes are recognized over the life of the underlying pool of contracts. As of March 31, 2006, we had a total managed automobile contract portfolio of approximately \$1,240.0 million, which included \$1,144.3 million of automobile contracts held by subsidiaries that are consolidated on our balance sheet and \$95.6 million of automobile contracts held by subsidiaries that are not consolidated on our balance sheet.

Our net income was \$1.8 million, or \$0.07 per diluted share, for the three months ended March 31, 2006, and \$3.4 million, or \$0.14 per diluted share, for the year ended December 31, 2005. As of March 31, 2006, we had \$75.6 million in shareholders' equity and \$1,354.2 million in total assets, of which \$1,050.8 million were net automobile receivables. During the three months ended March 31, 2006 and the year ended December 31, 2005, we purchased a total of \$255.6 million and \$691.3 million, respectively, of automobile contracts.

### **Our Business Strategy**



Our business objective is to maximize long-term profitability by efficiently purchasing and servicing sub-prime automobile contracts that generate strong and consistent risk-adjusted returns. We achieve this objective by employing our business strategy, which includes the following key elements:

**Disciplined Growth in Automobile Contract Purchases and Total Managed Portfolio.** We have focused on steady origination growth by expanding our network of marketing representatives. Since 2003, we have grown the number of marketing representatives from 42 as of December 31, 2003 to 84 as of March 31, 2006. We intend to continue to grow originations by further expansion of our marketing representative network, through increased

dealer penetration (that is, increasing automobile contract purchases from our current dealer base), and by developing new dealer relationships. We intend to increase dealer penetration through our recent initiatives to improve dealer service levels by decreasing our application turnaround and funding times. Our annual automobile finance contract purchases have grown from \$357.3 million in fiscal year 2003, to \$447.2 million in fiscal year 2004, to \$691.3 million in fiscal year 2005 and to \$801.5 million for the twelve months ended March 31, 2006, representing a compounded annual growth rate of 43.2%. Additionally, our managed portfolio increased from \$743.5 million as of December 31, 2003 to \$906.9 million as of December 31, 2004, to \$1,121.7 million as of December 31, 2005, and to \$1,240.0 million as of March 31, 2006, representing a compounded annual growth rate of 25.5%.

**Centralized Credit Underwriting Platform Focused on Disciplined Credit Management.** We underwrite all of our automobile contract purchases through a centralized process at our corporate headquarters in Irvine, California. We believe that a centralized underwriting approach enables us to maintain close control over the credit quality of our managed portfolio. During our underwriting process, we utilize a proprietary automated decisioning system that we have developed and continually enhanced over the last seven years. A major component of our automated system is a scorecard that we developed using the historical credit performance of our managed receivables portfolio. We also rely, to a lesser extent, on the judgment of our trained credit analysts to make risk-based credit and pricing decisions. Our high level of automation enhances our ability to make consistent credit decisions in a growth environment. Our credit performance has shown significant improvement with net charge-offs as a percentage of our average managed receivables portfolio equal to 6.8% for the year ended December 31, 2003, 7.8% for the year ended December 31, 2004, 5.3% for the year ended December 31, 2005, and 4.8% for the three months ended March 31, 2006.

**Geographically Focused Servicing Centers Allow Operating Flexibility and Drive Portfolio Performance.** We maintain four strategically located servicing centers across the country in California, Virginia, Florida, and Illinois. All four servicing centers are linked on-line with our automated collections system and accounts can be allocated between the different facilities as needed to optimize resource allocation. This strategy affords us solid time zone coverage, the ability to leverage the employee base in our four servicing locations and provides back-up capabilities for disaster scenarios. We have used performance benchmarking of the centers and internal disclosure of comparative performance data to encourage competition among our centers and to improve processes. We believe these techniques have contributed to improved delinquencies and charge-offs for the total managed portfolio.

**Securitization Funding Strategy and High-Quality Earnings.** We purchase automobile contracts with the intention of financing them on a long-term basis through asset-backed term securitizations. We have been a regular issuer of asset-backed securities since 1994, completing 40 asset-backed term securitizations totaling over \$4.3 billion through March 31, 2006. Our securitization funding strategy provides us with an attractive cost of matched funding and allows us to mitigate interest rate risk by locking in a fixed interest rate spread at the time of securitization, since the interest received on automobile contracts and interest paid for securitization notes payable are both fixed rate obligations. Additionally, since the third quarter of 2003, we have structured our securitizations to be treated for financial accounting purposes as secured financings, rather than as sales of automobile contracts. Generally, we expect that our revenues will grow proportionately to the size of our on-balance sheet portfolio of automobile contracts, thereby generating a recurring stream of interest income. We believe this securitization structure reduces the potential earnings volatility associated with accounting for securitizations as sales of automobile contracts, and as a result, has improved the quality of our earnings.

**Improved Operating Efficiency Gains Through Economies of Scale and Investments in Technology.** We believe that the use of technology in both our contract origination and servicing platforms has enabled us to achieve economies of scale as we have continued to grow our managed receivables portfolio. With our existing infrastructure, we expect to continue to be positioned to support future portfolio growth with slower increases in core operating expenses (that is, total expenses excluding provision for credit losses, interest expense and impairment loss on residual assets). Our core operating expenses as a percentage of average managed receivables have declined from 10.4% for the fiscal year 2003, to 8.4% for fiscal year 2004, 8.0% for fiscal year 2005 and 6.5% annualized for the three months ended March 31, 2006.



## **Recent Developments**

### ***Announcement of Second Quarter 2006 Financial Results***

On July 17, 2006, we announced our unaudited financial results for the second quarter ended June 30, 2006. Net income for the quarter ended June 30, 2006 was \$2.6 million, or \$0.11 per diluted share, compared to net income of \$545,000, or \$0.02 per diluted share, for the quarter ended June 30, 2005. Total revenues for the three months ended June 30, 2006 were \$67.2 million, an increase of \$19.4 million, or 40.7%, compared to \$47.8 million for the three months ended June 30, 2005. Total expenses for the three months ended June 30, 2006 were \$64.6 million, an increase of \$17.4 million, or 36.8%, compared to \$47.2 million for the three months ended June 30, 2005.

Net income for the six months ended June 30, 2006 was \$4.4 million, or \$0.18 per diluted share, compared to net income of \$306,000, or \$0.01 per diluted share, for the six months ended June 30, 2005. Total revenues for the six months ended June 30, 2006 were \$125.3 million, an increase of \$35.7 million, or 39.8%, compared to \$89.6 million for the six months ended June 30, 2005. Total expenses for the six months ended June 30, 2006 were \$120.8 million, an increase of \$31.5 million, or 35.3%, compared to \$89.3 million for the six months ended June 30, 2005.

During the second quarter of 2006, we purchased \$268.8 million of automobile contracts from dealers as compared to \$255.6 million during the first quarter of 2006 and \$153.9 million during the second quarter of 2005. As of June 30, 2006, our managed receivables totaled \$1,375.3 million compared to \$1,240.0 million as of March 31, 2006 and \$966.2 million as of June 30, 2005.

### ***Closing of Second Quarter 2006 Securitization***

On June 29, 2006, we closed the term securitization transaction for CPS Auto Receivables Trust 2006-B, issuing \$226.6 million of investment grade notes backed by \$257.5 million of automotive receivables originated by us. The transaction utilized a pre-funding structure, in which we sold approximately \$167.9 million of automobile receivables on June 29, 2006, and sold approximately \$89.6 million of additional automobile receivables on July 12, 2006. The \$226.6 million of notes, issued by CPS Auto Receivables Trust 2006-B, consisted of four classes and the weighted average effective coupon on those notes is approximately 5.77%.

### ***New Stock Option Plan***

On June 15, 2006, our shareholders approved a new long-term equity incentive plan, under which we may issue stock options or other equity incentives to our directors, officers and other employees, with respect to up to 1,500,000 shares of our common stock. We have not granted any incentives under this plan as of the date of this prospectus.

## **The Selling Shareholders**

### ***Levine Leichtman Capital Partners II, L.P.***

Levine Leichtman Capital Partners II, L.P., or Levine Leichtman, is one of our principal shareholders, and as of June 30, 2006 beneficially owned approximately 18.3% of the outstanding shares of our common stock. Levine Leichtman also holds \$40.0 million of our outstanding secured senior debt securities. Levine Leichtman was formed in 1997 and acquired its shares of our common stock in connection with a series of purchases of our debt securities beginning in October 1998. We entered into a registration rights agreement, as subsequently amended and restated, with Levine Leichtman to provide registration rights covering such shares. For more information, see **Selling Shareholders Registration Rights Agreement**.

### ***Stanwich Financial Services Corp.***

As of June 30, 2006, Stanwich Financial Services Corp., or Stanwich, beneficially owned approximately 2.5% of the outstanding shares of our common stock. Stanwich purchased a majority of its shares of our common stock from us in a private transaction in July 1998, and acquired additional shares in March 2000 in connection with the restructuring of certain of our debt obligations to Stanwich. We entered into various registration rights agreements, as subsequently amended and consolidated, with Stanwich to provide registration rights covering such shares. For more information, see Selling Shareholders Registration Rights Agreement.

For information regarding the beneficial ownership of our common stock by the selling shareholders as of June 30, 2006 and as adjusted to reflect the sale of the common stock in this offering by the selling shareholders, see Principal and Selling Shareholders.

### General Information

Our principal executive offices are located at 16355 Laguna Canyon Road, Irvine, California 92618, and our telephone number is (949) 753-6800. Our website is [www.consumerportfolio.com](http://www.consumerportfolio.com). None of the information on or hyperlinked from our website is incorporated by reference into this prospectus.

### The Offering

Common stock offered by us 500,000 shares (1)

Common stock offered by the selling shareholders 4,000,000 shares (1) (2)

Common stock to be outstanding after the offering 22,300,322 shares (1)(2) (3)

Use of proceeds We will receive the net proceeds from the sale of 500,000 shares of our common stock, and intend to use such net proceeds for the purchase of automobile contracts and for general corporate purposes. We will not receive any proceeds from the sale of shares by the selling shareholders.

Nasdaq National Market symbol CPSS

(1)

Excludes a 30-day option granted to the underwriter by us and by the selling shareholders to purchase up to 675,000 additional shares of common stock to cover over-allotments, if any. We granted an option to purchase up to 140,483 shares and the selling shareholders granted an option to purchase up to 534,517 shares.

(2)

Levine Leichtman is offering 3,500,000 shares and Stanwich is offering 500,000 shares of our common stock. In addition, Levine Leichtman granted to the underwriter an option to purchase up to 487,558 shares and Stanwich granted an option to purchase up to 46,959 shares of our common stock. The shares offered by Levine Leichtman include 1,000 shares that it may acquire upon exercise of a warrant.

(3)

Based on shares outstanding as of June 30, 2006. This share information does not include (a) 4,498,499 shares of common stock issuable upon the exercise of stock options outstanding as of June 30, 2006 at a weighted average exercise price of \$3.44 per share, (b) 272,000 shares issuable upon exercise of a warrant at an exercise price of \$4.85 per share, and (c) 1,657,131 additional shares reserved for future grants or issuances under our stock option plans. The number of shares issuable is subject to adjustment upon certain events, such as stock splits.



**[This page intentionally left blank.]**



**Summary Consolidated Financial Data**

The following table presents our summary consolidated financial data and operating data as of and for the dates indicated. The data under the captions **Statement of Operations Data** and **Balance Sheet Data** have been derived from our audited and unaudited consolidated financial statements. The remainder is derived from other records of ours.

You should read the summary consolidated financial data together with **Capitalization**, **Selected Consolidated Financial Data**, **Management's Discussion and Analysis of Financial Condition and Results of Operations** and our audited and unaudited financial statements and notes thereto that are included in this prospectus.

<b>Statement of Operations Data</b>	<b>As of and For the Three Months Ended March 31,</b>		<b>As of and For the Year Ended December 31,</b>		
(Dollars in thousands, except per share data)	<b>2006</b>	<b>2005</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>
	(unaudited)				
Revenues:					
Interest income	\$ 54,527	\$ 36,172	\$ 171,834	\$ 105,818	\$ 58,164
Servicing fees	1,005	2,264	6,647	12,480	17,058
Net gain on sale of contracts					10,421
Other income	2,492	3,397	15,216	14,394	19,343
Total revenues	58,024	41,833	193,697	132,692	104,986
Expenses:					
Employee costs	9,357	10,450	40,384	38,173	37,141
General and administrative	9,743	8,926	39,285	33,936	31,581
Interest expense	18,035	10,384	51,669	32,147	23,861
Provision for credit losses	19,099	12,312	58,987	32,574	11,390
Impairment loss on residual assets (1)				11,750	4,052
Total expenses	56,234	42,072	190,325	148,580	108,025
Income (loss) before income tax benefit	1,790	(239 )	3,372	(15,888 )	(3,039 )
Income tax benefit					(3,434 )
Net income (loss)	\$ 1,790	\$ (239 )	\$ 3,372	\$ (15,888 )	\$ 395
Earnings (loss) per share basic	\$ 0.08	\$ (0.01 )	\$ 0.16	\$ (0.75 )	\$ 0.02
Earnings (loss) per share diluted	\$ 0.07	\$ (0.01 )	\$ 0.14	\$ (0.75 )	\$ 0.02
Weighted average shares outstanding basic	21,732	21,528	21,627	21,111	20,263

Weighted average shares outstanding diluted	24,188	21,528	23,513	21,111	21,578
<b>Balance Sheet Data</b>					
Total assets	\$ 1,354,223	\$ 850,533	\$ 1,155,144	\$ 766,599	\$ 492,470
Cash and cash equivalents	25,504	9,730	17,789	14,366	33,209
Restricted cash and equivalents	212,428	150,059	157,662	125,113	67,277
Finance receivables, net	1,050,825	620,302	913,576	550,191	266,189
Residual interest in securitizations	22,608	44,135	25,220	50,430	111,702
Warehouse lines of credit	75,056	50,535	35,350	34,279	33,709
Residual interest financing	37,728	16,411	43,745	22,204	
Securitization trust debt	1,100,606	619,430	924,026	542,815	245,118
Long-term debt	46,314	73,829	58,655	74,829	102,465
Shareholders equity	\$ 75,626	\$ 69,808	\$ 73,589	\$ 69,920	\$ 82,160

(Dollars in thousands, except per share data)	<b>As of and For the Three Months Ended March 31,</b>		<b>As of and For the Year Ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>
	(unaudited)				
<b>Contract Purchases/Securitized</b>					
Automobile contract purchases	255,586	144,165	691,252	447,232	357,320
Automobile contract acquisitions (2)				74,901	152,143
Automobile contracts securitized structured as sales					254,436
Automobile contracts securitized structured as secured financings	245,000	137,390	698,353	491,269	162,488
<b>Managed Portfolio Data</b>					
Contracts held by consolidated subsidiaries	\$ 1,144,340	\$ 691,967	\$ 1,000,597	\$ 619,794	\$ 317,952
Contracts held by non-consolidated subsidiaries	83,162	193,823	103,130	233,621	425,534
SeaWest third party portfolio (3)	12,456	40,501	18,018	53,463	
Total managed portfolio	\$ 1,239,958	\$ 926,291	\$ 1,121,745	\$ 906,878	\$ 743,485
Average managed portfolio	1,191,132	915,547	997,697	861,261	674,523
Weighted average fixed effective interest rate (total managed portfolio) (4)	18.6 %	19.0 %	18.6 %	19.2 %	19.7 %
Core operating expense (% of average managed portfolio) (5)	6.5 %	8.5 %	8.0 %	8.4 %	10.4 %
Allowance for loan losses	\$ 63,846	\$ 46,284	\$ 57,728	\$ 42,615	\$ 35,889
Allowance for loan losses (% of total contracts held by consolidated subsidiaries)	5.6 %	6.7 %	5.8 %	6.9 %	11.3 %
Total delinquencies (% of total managed portfolio) (6)	1.8 %	2.1 %	3.8 %	4.0 %	4.7 %
Total delinquencies and repossessions (% of total managed portfolio) (6)	2.7 %	3.2 %	5.0 %	5.6 %	6.2 %
Net charge-offs (% of average	4.8 %	6.6 %	5.3 %	7.8 %	6.8 %

managed portfolio) (4)(7)

(1)

The impairment loss was related to our analysis and estimate of the expected ultimate performance of our previously securitized pools that were held by our non-consolidated subsidiaries and the residual interest in securitizations. The impairment loss was a result of the actual net loss and prepayment rates exceeding our previous estimates for the automobile contracts held by our non-consolidated subsidiaries.

(2)

Represents automobile contracts not purchased directly from dealers, but acquired as a result of our acquisitions of TFC in 2003 and of certain assets of SeaWest in 2004.

(3)

Receivables related to the SeaWest third party portfolio, on which we earn only a servicing fee.

(4)

Excludes receivables related to the SeaWest third party portfolio.

(5)

Total expenses excluding provision for credit losses, interest expense and impairment loss on residual assets.

(6)

For further information regarding delinquencies and the managed portfolio, see the table captioned *Delinquency Experience*, at page 45 of this prospectus and the notes to that table.

(7)

Net charge-offs include the remaining principal balance, after the application of the net proceeds from the liquidation of the vehicle (excluding accrued and unpaid interest) and amounts collected subsequent to the date of the charge-off. For further information regarding charge-offs, see the table captioned *Net Charge-Off Experience*, at page 46 of this prospectus and the notes to that table.

## RISK FACTORS

This offering involves a high degree of risk. You should carefully consider the risks described below and the other information in this prospectus and the information incorporated by reference before deciding to invest in our common stock. Our business, operating results and financial condition could be adversely affected by any of the following specific risks. The trading price of our common stock could decline due to any of these risks and other industry risks, and you could lose all or part of your investment. In addition to the risks described below, we may encounter risks that are not currently known to us or that we currently deem immaterial, which may also impair our business operations and your investment in our common stock.

### Risks Related To Our Business

*We require a substantial amount of cash to service our substantial debt.*

To service our existing substantial indebtedness, we require a significant amount of cash. Our ability to generate cash depends on many factors, including our successful financial and operating performance. Our financial and operational performance depends upon a number of factors, many of which are beyond our control. These factors include, without limitation:

- the economic and competitive conditions in the asset-backed securities market;
- the performance of our current and future automobile contracts;
- the performance of our residual interests from our securitizations and warehouse credit facilities;
- any operating difficulties or pricing pressures we may experience;
- our ability to obtain credit enhancement for our securitizations;
- our ability to establish and maintain dealer relationships;
- the passage of laws or regulations that affect us adversely;
- our ability to compete with our competitors; and

- 

our ability to acquire and finance automobile contracts.

Depending upon the outcome of one or more of these factors, we may not be able to generate sufficient cash flow from operations or obtain sufficient funding to satisfy all of our obligations. If we were unable to pay our debts, we would be required to pursue one or more alternative strategies, such as selling assets, refinancing or restructuring our indebtedness or selling additional equity capital. These alternative strategies might not be feasible at the time, might prove inadequate or could require the prior consent of our secured and unsecured lenders.

***We need substantial liquidity to operate our business.***

We have historically funded our operations principally through internally generated cash flows, sales of debt and equity securities, including through securitizations and warehouse credit facilities, borrowings from the selling shareholders and sales of subordinated notes. However, we may not be able to obtain sufficient funding for our future operations from such sources. If we were unable to access the capital markets or obtain other acceptable financing, our results of operations, financial condition and cash flows would be materially and adversely affected. We require a substantial amount of cash liquidity to operate our business. Among other things, we use such cash liquidity to:

- 

acquire automobile contracts;

- 

fund overcollateralization in warehouse credit facilities and securitizations;

- 

pay securitization fees and expenses;

- 

fund spread accounts in connection with securitizations;

- 

satisfy working capital requirements and pay operating expenses; and

- 

pay interest expense.

Prior to the third quarter of 2003, we reported a gain on the sale of our automobile contracts upon their securitization. This gain represented a substantial portion of our revenues prior to the third quarter of 2003. However, although we reported this gain at the time of sale, we received the monthly cash payments on those contracts (representing revenue previously recognized) over the life of the automobile contracts, rather than at the time of sale. As a result, a substantial portion of our reported revenues prior to the third quarter of 2003 did not represent immediate cash liquidity.

***Our results of operations will depend on our ability to secure and maintain adequate credit and warehouse financing on favorable terms.***

We depend on warehouse credit facilities to finance our purchases of automobile contracts. Our business strategy requires that these warehouse credit facilities continue to be available to us from the time of purchase or origination of an automobile contract until it is financed through a securitization.

Our primary sources of day-to-day liquidity are our warehouse credit facilities, in which we sell and contribute automobile contracts, as often as twice a week, to affiliated special-purpose entities, where they are warehoused until they are securitized, at which time funds advanced under one or more warehouse credit facilities are repaid from the proceeds of the securitizations. The special-purpose entities obtain the funds to purchase these contracts by pledging the contracts to a trustee for the benefit of warehouse lenders, who advance funds to our affiliated special-purpose entities based on the dollar amount of the contracts pledged. We depend substantially on two warehouse credit facilities: (i) a \$150 million warehouse credit facility, which we established in November 2005 and, unless earlier renewed or terminated upon the occurrence of certain events will expire in November 2006 and (ii) a \$200 million warehouse credit facility, which we established in June 2004 and, unless renewed or earlier terminated upon the occurrence of certain events, will expire in June 2007. Each of these facilities may be renewed by mutual agreement between the lender and us. These warehouse credit facilities will remain available to us only if, among other things, we comply with certain financial covenants contained in the documents governing these facilities. These warehouse credit facilities may not be available to us in the future and we may not be able to obtain other credit facilities on favorable terms to fund our operations.

If we were unable to arrange new warehousing or other credit facilities or renew our existing warehouse credit facilities when they come due, our results of operations, financial condition and cash flows would be materially and adversely affected.

***Our results of operations will depend on our ability to securitize our portfolio of automobile contracts.***

We are dependent upon our ability to continue to finance pools of automobile contracts in securitizations in order to generate cash proceeds for new purchases of automobile contracts. We have historically depended on securitizations of automobile contracts to provide permanent financing of those contracts. By permanent financing we mean financing that extends to cover the full term during which the underlying contracts are outstanding. By contrast, our warehouse credit facilities permit us to borrow against the value of such receivables only for limited periods of time. Our past practice and future plan has been and is to repay loans made to us under our warehouse credit facilities with the proceeds of securitizations. There can be no assurance that any securitization transaction will be available on terms acceptable to us, or at all. The timing of any securitization transaction is affected by a number of factors beyond our control, any of which could cause substantial delays, including, without limitation:

- 

market conditions;

-

the approval by all parties of the terms of the securitization;

- 

the availability of credit enhancement on acceptable terms; and

- 

our ability to acquire a sufficient number of automobile contracts for securitization.

Adverse changes in the market for securitized pools of automobile contracts may result in our inability to securitize automobile contracts and may result in a substantial extension of the period during which our automobile contracts are financed through our warehouse credit facilities, which would burden our financing capabilities, could require us to curtail our purchase of, or find an alternative source of financing for, such automobile contracts and would have a material adverse effect on our results of operations.



***Our results of operations will depend on cash flows from our residual interests in our securitization program and our warehouse credit facilities.***

When we finance our automobile contracts through securitizations and warehouse credit facilities, we receive cash and a residual interest in the assets financed. Those financed assets are owned by the special-purpose subsidiary that is formed for the related securitization. This residual interest represents the right to receive the future cash flows to be generated by the automobile contracts in excess of (i) the interest and principal paid to investors on the indebtedness issued in connection with the financing (ii) the costs of servicing the contracts and (iii) certain other costs incurred in connection with completing and maintaining the securitization or warehouse credit facility. We sometimes refer to these future cash flows as excess spread cash flows.

Under the financial structures we have used to date in our securitizations and warehouse credit facilities, excess spread cash flows that would otherwise be paid to the holder of the residual interest are first used to increase overcollateralization or are retained in a spread account within the securitization trusts or the warehouse facility to provide liquidity and credit enhancement for the related securities.

While the specific terms and mechanics vary among transactions, our securitization and warehousing agreements generally provide that we will receive excess spread cash flows only if the amount of overcollateralization and spread account balances have reached specified levels and/or the delinquency, defaults or net losses related to the contracts in the automobile contract pools are below certain predetermined levels. In the event delinquencies, defaults or net losses on contracts exceed these levels, the terms of the securitization or warehouse credit facility:

- 

may require increased credit enhancement, including an increase in the amount required to be on deposit in the spread account, to be accumulated for the particular pool;

- 

may restrict the distribution to us of excess spread cash flows associated with other securitized or warehoused pools; and

- 

in certain circumstances, may permit affected parties to require the transfer of servicing on some or all of the securitized or warehoused contracts from us to an unaffiliated servicer.

We typically retain or sell residual interests or use them as collateral to borrow cash. In any case, the future excess spread cash flow received in respect of the residual interests are integral to the financing of our operations. The amount of cash received from residual interests depends in large part on how well our portfolio of securitized and warehoused automobile contracts performs. If our portfolio of securitized and warehoused automobile contracts has higher delinquency and loss ratios than expected, then the amount of money realized from our retained residual interests, or the amount of money we could obtain from the sale or other financing of our residual interests, would be reduced, which could have an adverse effect on our operations, financial condition and cash flows.

***If we are unable to obtain credit enhancement for our securitizations or our warehouse credit facilities upon favorable terms, our results of operations would be impaired.***

In our securitizations, we typically utilize credit enhancement in the form of one or more financial guaranty insurance policies issued by financial guaranty insurance companies. Each of these policies unconditionally and irrevocably guarantees certain interest and principal payments on the senior classes of the securities issued in our securitizations.

These guarantees enable these securities to achieve the highest credit rating available. This form of credit enhancement reduces the costs of our securitizations relative to alternative forms of credit enhancement currently available to us. None of such financial guaranty insurance companies is required to insure future securitizations. As we pursue future securitizations, we may not be able to obtain:

- 

credit enhancement in any form from financial guaranty insurance companies or any other provider of credit enhancement on terms acceptable to us, or at all; or

- 

similar ratings for senior classes of securities to be issued in future securitizations.

If we were unable to obtain such enhancements or such ratings, we would expect to incur increased interest expense, which would adversely affect our results of operations.

***If we are unable to successfully compete with our competitors, our results of operations may be impaired.***

The automobile financing business is highly competitive. We compete with a number of national, regional and local finance companies. In addition, competitors or potential competitors include other types of financial services companies, such as commercial banks, savings and loan associations, leasing companies, credit unions providing retail loan financing and lease financing for new and used vehicles and captive finance companies affiliated with major automobile manufacturers such as General Motors Acceptance Corporation and Ford Motor Credit Corporation. Many of our competitors and potential competitors possess substantially greater financial, marketing, technical, personnel and other resources than we do, including greater access to capital markets for unsecured commercial paper and investment grade rated debt instruments, and to other funding sources which may be unavailable to us. Moreover, our future profitability will be directly related to the availability and cost of our capital relative to that of our competitors. Many of these companies also have long-standing relationships with automobile dealers and may provide other financing to dealers, including floor plan financing for the dealers' purchases of automobiles from manufacturers, which we do not offer. There can be no assurance that we will be able to continue to compete successfully and, as a result, we may not be able to purchase contracts from dealers at a price acceptable to us, which could result in reductions in our revenues or the cash flows available to us.

***If our dealers do not submit a sufficient number of suitable automobile contracts to us for purchase, our results of operations may be impaired.***

We are dependent upon establishing and maintaining relationships with a large number of unaffiliated automobile dealers to supply us with automobile contracts. During the year ended December 31, 2005, no dealer accounted for more than 1.0% of the contracts we purchased. The agreements we have with dealers to purchase contracts do not require dealers to submit a minimum number of contracts for purchase. The failure of dealers to submit contracts that meet our underwriting criteria could result in reductions in our revenues or the cash flows available to us, and, therefore, could have an adverse effect on our results of operations.

***If a significant number of our automobile contracts prepay or experience defaults, our results of operations may be impaired.***

We specialize in the purchase and servicing of contracts to finance automobile purchases by sub-prime customers, those who have limited credit history, low income, or past credit problems. Such contracts entail a higher risk of non-performance, higher delinquencies and higher losses than contracts with more creditworthy customers. While we believe that our pricing of the automobile contracts and the underwriting criteria and collection methods we employ enable us to control, to a degree, the higher risks inherent in contracts with sub-prime customers, no assurance can be given that such pricing, criteria and methods will afford adequate protection against such risks. We have in the past experienced fluctuations in the delinquency and charge-off performance of our contracts.

If automobile contracts that we purchase or service are prepaid or experience defaults to a greater extent than we have anticipated, this could materially and adversely affect our results of operations, financial condition, cash flows and liquidity. Our results of operations, financial condition, cash flows and liquidity, depend, to a material extent, on the performance of automobile contracts that we purchase, warehouse and securitize. A portion of the automobile contracts acquired by us will default or prepay. In the event of payment default, the collateral value of the vehicle securing an automobile contract realized by us in a repossession will most likely not cover the outstanding principal balance on that contract and the related costs of recovery. We maintain an allowance for credit losses on automobile contracts held on our balance sheet, which reflects our estimates of probable credit losses that can be reasonably estimated for securitizations that are accounted for as financings and warehoused contracts. If the allowance is inadequate, then we would recognize the losses in excess of the allowance as an expense and our results of operations could be adversely affected. In addition, under the terms of our warehouse credit facilities, we are not able to borrow against defaulted automobile contracts, including contracts that are, at the time of default, funded under our warehouse credit facilities, which will reduce the overcollateralization of those warehouse credit facilities and possibly reduce the

amount of cash flows available to us.

Our servicing income can also be adversely affected by prepayment of, or defaults under, automobile contracts in our servicing portfolio. Our contractual servicing revenue is based on a percentage of the outstanding principal balance of the automobile contracts in our servicing portfolio. If automobile contracts are prepaid or charged off, then our servicing revenue will decline, while our servicing costs may not decline proportionately. In addition

unexpected levels of defaults or losses may trigger changes in the terms applicable to our securitizations and warehouse credit facilities, which could adversely affect our cash flows, our revenues, or both.

The value of our residual interest in the securitized assets in each securitization treated as a sale for financial accounting purposes (securitizations entered into prior to the beginning of the third quarter of 2003) reflects our estimate of expected future credit losses and prepayments for the automobile contracts included in that securitization. If actual rates of credit loss or prepayments, or both, on such automobile contracts exceed our estimates, the value of our residual interest and the related cash flow would be impaired, and we would be required to record an impairment charge, which would reduce our earnings. We periodically review our credit loss and prepayment assumptions relative to the performance of the securitized automobile contracts and to market conditions. Our results of operations and liquidity could be adversely affected if actual credit loss or prepayment levels on securitized automobile contracts substantially exceed anticipated levels.

Higher credit losses than anticipated could also result in adverse changes in the structure of future securitization transactions, such as a requirement of increased cash collateral or other credit enhancement in such transactions.

***If we lose servicing rights on our portfolio of automobile contracts, our results of operations will be impaired.***

We are entitled to receive servicing fees only while we act as servicer under the applicable sale and servicing agreements governing our warehouse facilities and securitizations. Under such agreements, we may be terminated as servicer upon the occurrence of certain events, including:

- 

our failure generally to observe and perform covenants and agreements applicable to us;

- 

certain bankruptcy events involving us; or

- 

the occurrence of certain events of default under the documents governing the facilities.

The loss of our servicing rights could materially and adversely affect our results of operations, financial condition and cash flows. Our results of operations, financial condition and cash flows, would be materially and adversely affected if we were to be terminated as servicer with respect to a material portion of the automobile contracts for which we are receiving servicing fees.

***If we lose key personnel, our results of operations may be impaired.***

Our management team averages eleven years of service with us. Charles E. Bradley, Jr., our President and CEO, has been our President since our formation in 1991. Our future operating results depend in significant part upon the continued service of our key senior management personnel, none of whom is bound by an employment agreement. Our future operating results also depend in part upon our ability to attract and retain qualified management, technical, sales and support personnel for our operations. Competition for such personnel is intense. We cannot assure you that we will be successful in attracting or retaining such personnel. The loss of any key employee, the failure of any key employee to perform in his or her current position or our inability to attract and retain skilled employees, as needed, could materially and adversely affect our results of operations, financial condition and cash flows.

***If we fail to comply with regulations, our results of operations may be impaired.***

Failure to materially comply with all laws and regulations applicable to us could materially and adversely affect our ability to operate our business. Our business is subject to numerous federal and state consumer protection laws and regulations, which, among other things:

- require us to obtain and maintain certain licenses and qualifications;
- limit the interest rates, fees and other charges we are allowed to charge;
- limit or prescribe certain other terms of our automobile contracts;
- require specific disclosures to our customers;
- define our rights to repossess and sell collateral; and
- maintain safeguards designed to protect the security and confidentiality of customer information.

We believe that we are in compliance in all material respects with all such laws and regulations, and that such laws and regulations have had no material adverse effect on our ability to operate our business. However, we may be materially and adversely affected if we fail to comply with:

- applicable laws and regulations;
- changes in existing laws or regulations;
- changes in the interpretation of existing laws or regulations; or
- any additional laws or regulations that may be enacted in the future.

***If we experience unfavorable litigation results, our results of operations may be impaired.***

Unfavorable outcomes in any of our current or future litigation proceedings could materially and adversely affect our results of operations, financial conditions and cash flows. As a consumer finance company, we are subject to various consumer claims and litigation seeking damages and statutory penalties based upon, among other things, disclosure inaccuracies and wrongful repossession, which could take the form of a plaintiff's class action complaint. We, as the assignee of finance contracts originated by dealers, may also be named as a co-defendant in lawsuits filed by consumers principally against dealers. We are also subject to other litigation common to the automobile industry and businesses in general. The damages and penalties claimed by consumers and others in these types of matters can be substantial. The relief requested by the plaintiffs varies but includes requests for compensatory, statutory and punitive damages.

While we intend to vigorously defend ourselves against such proceedings, there is a chance that our results of operations, financial condition and cash flows could be materially and adversely affected by unfavorable outcomes.

***If we experience problems with our originations, accounting or collection systems, our results of operations may be impaired.***

We are dependent on our receivables originations, accounting and collection systems to service our portfolio of automobile contracts. Such systems are vulnerable to damage or interruption from natural disasters, power loss, telecommunication failures, terrorist attacks, computer viruses and other events. A significant number of our systems are not redundant, and our disaster recovery planning is not sufficient for every eventuality. Our systems are also subject to break-ins, sabotage and intentional acts of vandalism by internal employees and contractors as well as third parties. Despite any precautions we may take, such problems could result in interruptions in our services, which could harm our reputation and financial condition. We do not carry business interruption insurance sufficient to compensate us for losses that may result from interruptions in our service as a result of system failures. Such systems problems could materially and adversely affect our results of operations, financial conditions and cash flows.

***We may be exposed to potential risks if we do not have an effective system of disclosure controls or internal controls or fail to comply fully with section 404 of Sarbanes-Oxley.***

We have not yet completed a review of our internal controls over financial reporting, which we are required to complete under Section 404 of the Sarbanes Oxley Act of 2002 by the end of 2006. We anticipate devoting significant management time and resources to documenting and improving our internal controls over financial reporting. We cannot be certain that we will implement and maintain adequate controls over our financial reporting in the future. If we fail to maintain an effective system of disclosure controls or internal control over financial reporting, including satisfaction of the requirements of Section 404 of the Sarbanes Oxley Act of 2002, we may not be able to accurately or timely report on our financial results or adequately identify and reduce fraud. Were that to happen, our financial position could be harmed, current and future shareholders could lose confidence in our business, our reported financial information, or both, which could have a negative effect on our trading price; and we could be exposed to litigation or regulatory proceedings, which may be costly or divert management attention.

***We have substantial indebtedness.***

We have and will continue to have a substantial amount of indebtedness. At March 31, 2006, we had approximately \$1,259.9 million of debt outstanding. Such debt consisted primarily of \$1,100.6 million of securitization trust debt and \$75.1 million of warehouse indebtedness, and also included \$40.0 million owed to one



of the selling shareholders, and \$6.3 million owed under a subordinated notes program. We are also currently offering the subordinated notes to the public on a continuous basis, and such notes have maturities that range from three months to ten years.

Our substantial indebtedness could adversely affect our financial condition by, among other things:

- increasing our vulnerability to general adverse economic and industry conditions;
- requiring us to dedicate a substantial portion of our cash flow from operations payments on our indebtedness, thereby reducing amounts available for working capital, capital expenditures and other general corporate purposes;
- limiting our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate;
- placing us at a competitive disadvantage compared to our competitors that have less debt; and
- limiting our ability to borrow additional funds.

Although we believe we will generate sufficient free cash flow to service such debt, there is no assurance that we will be able to do so. If we do not generate sufficient operating profits, our ability to make required payments on our debt would be impaired.

***Because we are subject to many restrictions in our existing credit facilities and securitization transactions, our ability to pay dividends or engage in specified transactions may be impaired.***

The terms of our existing credit facilities and our outstanding debt impose significant operating and financial restrictions on us and our subsidiaries and require us to meet certain financial tests. These restrictions may have an adverse effect on our business activities, results of operations and financial condition. These restrictions may also significantly limit or prohibit us from engaging in certain transactions, including the following:

- incurring or guaranteeing additional indebtedness;
- making capital expenditures in excess of agreed upon amounts;
- paying dividends or other distributions to our stockholders or redeeming, repurchasing or retiring our capital stock or subordinated obligations;

- making investments;
- creating or permitting liens on our assets or the assets of our subsidiaries;
- issuing or selling capital stock of our subsidiaries;
- transferring or selling our assets;
- engaging in mergers or consolidations;
- permitting a change of control of our company;
- liquidating, winding up or dissolving our company;
- changing our name or the nature of our business, or the names or nature of the business of our subsidiaries; and
- engaging in transactions with our affiliates outside the normal course of business.

These restrictions may limit our ability to obtain additional sources of capital, which may limit our ability to generate earnings. In addition, the failure to comply with any of the covenants of our existing credit facilities or to maintain certain indebtedness ratios would cause a default under one or more of our credit facilities or our other debt agreements that may be outstanding from time to time. A default, if not waived, could result in acceleration of the related indebtedness, in which case such debt would become immediately due and payable. A continuing default or acceleration of one or more of our credit facilities or any other debt agreement, would likely cause a default under other debt agreements that otherwise would not be in default, in which case all such related indebtedness could be accelerated. If this occurs, we may not be able to repay our debt or borrow sufficient funds to refinance our



indebtedness. Even if any new financing is available, it may not be on terms that are acceptable to us or it may not be sufficient to refinance all of our indebtedness as it becomes due.

In addition, the transaction documents for our securitizations restrict our securitization subsidiaries from declaring or making payment to us of (i) any dividend or other distribution on or in respect of any shares of their capital stock, or (ii) any payment on account of the purchase, redemption, retirement or acquisition of any option, warrant or other right to acquire shares of their capital stock unless (in each case) at the time of such declaration or payment (and after giving effect thereto) no amount payable under any transaction document with respect to the related securitization is then due and owing, but unpaid. These restrictions may limit our ability to receive distributions in respect of the residual interests from our securitization facilities, which may limit our ability to generate earnings.

### **Risks Related to General Factors**

*If the economy of all or certain regions of the United States slows or enters into a recession, our results of operations may be impaired.*

Our business is directly related to sales of new and used automobiles, which are sensitive to employment rates, prevailing interest rates and other domestic economic conditions. Delinquencies, repossessions and losses generally increase during economic slowdowns or recessions. Because of our focus on sub-prime customers, the actual rates of delinquencies, repossessions and losses on our automobile contracts could be higher under adverse economic conditions than those experienced in the automobile finance industry in general, particularly in the states of Texas, California, Ohio, Florida, Pennsylvania and Louisiana, states in which our automobile contracts are geographically concentrated. Any sustained period of economic slowdown or recession could adversely affect our ability to acquire suitable contracts, or to securitize pools of such contracts. The timing of any economic changes is uncertain, and weakness in the economy could have an adverse effect on our business and that of the dealers from which we purchase contracts and result in reductions in our revenues or the cash flows available to us.

*Our results of operations may be impaired as a result of natural disasters.*

Our automobile contracts are geographically concentrated in the states of Texas, California, Ohio, Florida, Pennsylvania, and Louisiana. Several of such states are particularly susceptible to natural disasters: earthquake in the case of California, and hurricanes and flooding in the states of Florida, Texas and Louisiana. Natural disasters, in those states or others, could cause a material number of our vehicle purchasers to lose their jobs, or could damage or destroy vehicles that secure our automobile contracts. In either case, such events could result in our receiving reduced collections on our automobile contracts, and could thus result in reductions in our revenues or the cash flows available to us.

*If an increase in interest rates results in a decrease in our cash flow from excess spread, our results of operations may be impaired.*

Our profitability is largely determined by the difference, or spread, between the effective interest rate received by us on the automobile contracts that we acquire and the interest rates payable under our warehouse credit facilities and on the asset-backed securities issued in our securitizations.

Several factors affect our ability to manage interest rate risk. Specifically, we are subject to interest rate risk during the period between when automobile contracts are purchased from dealers and when such contracts are sold and financed in a securitization. Interest rates on our warehouse credit facilities are adjustable while the interest rates on the automobile contracts are fixed. Therefore, if interest rates increase, the interest we must pay to the lenders under our warehouse credit facilities is likely to increase while the interest realized by us from those warehoused automobile contracts remains the same, and thus, during the warehousing period, the excess spread cash flow received by us would likely decrease. Additionally, contracts warehoused and then securitized during a rising interest rate

environment may result in less excess spread cash flow realized by us under those securitizations as, historically, our securitization facilities pay interest to securityholders on a fixed rate basis set at prevailing interest rates at the time of the closing of the securitization, which may be several months after the securitized contracts were originated and entered the warehouse, while our customers pay fixed rates of interest on the contracts, set at the time they purchase the underlying vehicles. A decrease in excess spread cash flow could adversely affect our earnings and cash flow.

To mitigate, but not eliminate, the short-term risk relating to interest rates payable by us under the warehouse facilities, we generally hold automobile contracts in the warehouse credit facilities for less than four months. To mitigate, but not eliminate, the long-term risk relating to interest rates payable by us in securitizations, we have in the past, and intend to continue to, structure some of our securitization transactions to include pre-funding structures, whereby the amount of securities issued exceeds the amount of contracts initially sold into the securitization. In pre-funding, the proceeds from the pre-funded portion are held in an escrow account until we sell the additional contracts into the securitization in amounts up to the balance of the pre-funded escrow account. In pre-funded securitizations, we effectively lock in our borrowing costs with respect to the contracts we subsequently sell into the securitization. However, we incur an expense in pre-funded securitizations equal to the difference between the money market yields earned on the proceeds held in escrow prior to subsequent delivery of contracts and the interest rate paid on the securities issued in the securitization. The amount of such expense may vary. Despite these mitigation strategies, an increase in prevailing interest rates would cause us to receive less excess spread cash flows on automobile contracts, and thus could adversely affect our earnings and cash flows.

***The effects of terrorism and military action may impair our results of operations.***

The long-term economic impact of the events of September 11, 2001, possible future terrorist attacks or other incidents and related military action, or current or future military action by United States forces in Iraq and other regions, could have a material adverse effect on general economic conditions, consumer confidence, and market liquidity in the United States. No assurance can be given as to the effect of these events on the performance of our automobile contracts. Any adverse impact resulting from these events could materially affect our results of operations, financial condition and cash flows. In addition, activation of a substantial number of U.S. military reservists or members of the National Guard may significantly increase the proportion of contracts whose interest rates are reduced by the application of the Servicemembers' Civil Relief Act, which provides, generally, that an obligor who is covered by that act may not be charged interest on the related contract in excess of 6% annually during the period of the obligor's active duty.

**Risks Related to Our Common Stock**

***Our common stock is thinly-traded.***

Our stock is thinly-traded, which means investors will have limited opportunities to sell their shares of common stock in the open market. Limited trading of our common stock also contributes to more volatile price fluctuations. Because there historically has been low trading volume in our common stock, there can be no assurance that our stock price will not decline as additional shares are sold in the public market. As of June 30, 2006, all of our directors and executive officers and the selling shareholders beneficially owned 10,728,292 shares of our common stock, or approximately 44.7%. Following this offering, and assuming the underwriter does not exercise its over-allotment option, this group will beneficially own 6,728,292 shares of our common stock, or approximately 27.4%. See Principal and Selling Shareholders.

***We do not intend to pay dividends on our common stock.***

We have never declared or paid any cash dividends on our common stock. We currently intend to retain any future earnings and do not expect to pay any dividends in the foreseeable future. Even if we were to change our intention, the terms of our secured debt prohibit us from paying any dividends to our shareholders without the consent of the holder of such secured debt, which may be withheld in its sole discretion. See Dividend Policy.



## FORWARD-LOOKING STATEMENTS

Discussions of certain matters contained in this prospectus and incorporated herein by reference may constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act ) and Section 21E of the Exchange Act, and as such, may involve risks and uncertainties. These forward-looking statements relate to, among other things, expectations of the business environment in which we operate, projections of future performance, perceived opportunities in the market and statements regarding our mission and vision. You can generally identify forward-looking statements as statements containing the words will, would, believe, may, could, expect, anticipate, intend, estimate, assume or other similar expressions. Results, performance and achievements may differ materially from the results, performance and achievements expressed or implied in such forward-looking statements. The discussion under Risk Factors identifies some of the factors that might cause such a difference, including the following:

- changes in general economic conditions;
- changes in interest rates;
- our ability to generate sufficient operating and financing cash flows;
- competition;
- level of future provisioning for receivables losses; and
- regulatory requirements.

Forward-looking statements are not guarantees of performance. They involve risks, uncertainties and assumptions. Actual results may differ from expectations due to many factors beyond our ability to control or predict, including those described herein, and in documents incorporated by reference in this prospectus. For these statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

We undertake no obligation to publicly update any forward-looking information. You are advised to consult any additional disclosure we make in our periodic reports filed with the SEC. See Where You Can Find More Information and Documents Incorporated by Reference.

## USE OF PROCEEDS

We estimate that the net proceeds we will receive from the sale of 500,000 shares of our common stock in this offering will be approximately \$3.1 million, assuming a public offering price of \$7.00 per share (based on the last



reported sale price of our common stock on July 18, 2006), after deducting the underwriting discounts and commissions and estimated offering expenses of approximately \$170,000 payable by us. If the underwriter's over-allotment option is exercised in full, we estimate that the net proceeds from our sale of 640,483 shares of our common stock will be approximately \$4.1 million. We intend to use the net proceeds we receive from this offering to purchase automobile contracts and for general corporate purposes. We will not receive any of the proceeds from the sale by the selling shareholders in this offering of 4,000,000 shares of our common stock (or 4,534,517 shares if the underwriter's over-allotment option is exercised in full).

**PRICE RANGE OF COMMON STOCK**

Our common stock has been quoted on the Nasdaq National Market under the symbol CPSS since our initial public offering in 1992. The following table shows for the periods indicated the high and low sale prices per share of our common stock.

	<b>High</b>	<b>Low</b>
<b>2004</b>		
First quarter	\$ 3.96	\$ 2.94
Second quarter	4.97	3.12
Third quarter	5.21	3.71
Fourth quarter	4.87	3.98
<b>2005</b>		
First quarter	5.50	4.26
Second quarter	5.38	3.50
Third quarter	5.45	4.14
Fourth quarter	6.50	4.82
<b>2006</b>		
First quarter	8.50	5.30
Second quarter	8.84	6.04
Third quarter (through July 18, 2006)	7.53	6.17

On July 18, 2006, the last reported sale price of our common stock on the Nasdaq National Market was \$7.00 per share. As of June 30, 2006, we had approximately 81 shareholders of record of our common stock.

**DIVIDEND POLICY**

We have not declared or paid any cash dividends on our common stock since inception.

We currently anticipate that we will retain all future earnings for use in our business and do not anticipate that we will pay any cash dividends in the foreseeable future. The payment of any future dividends will be at the discretion of our Board of Directors and will depend upon, among other things, future earnings, operations, capital requirements and our general financial condition, general business conditions and contractual restrictions on payment of dividends, if any.

Our agreements relating to the \$40.0 million of our debt securities held by one of the selling shareholders prohibit us from paying dividends (or other distributions on and repurchases of our common stock) so long as such debt remains outstanding, without the consent of that selling shareholder.



**CAPITALIZATION**

The following table sets forth our capitalization, as of March 31, 2006:

- 

on an actual basis; and

- 

on an as adjusted basis to give effect to the sale by us of 500,000 shares of common stock in this offering at an assumed offering price of \$7.00 per share, the last reported sale price of our common stock on July 18, 2006, after deducting underwriting discounts and commissions and estimated offering expenses payable by us.

**As of March 31, 2006 (1)**

(Dollars in thousands)

	<b>Actual</b>	<b>As Adjusted</b>
		(unaudited)
Cash and cash equivalents	\$ 25,504	\$ 28,642
Long-term debt:		
Senior secured debt, related party	\$ 40,000	\$ 40,000
Subordinated renewable notes (2)	6,314	6,314
Total long-term debt (2)(3)	46,314	46,314
Shareholders' equity:		
Preferred stock, \$1.00 par value; authorized 10,000,000 shares in series; none outstanding		
Common stock, no par value; authorized 30,000,000 shares; 21,819,333 shares issued and outstanding, actual; 22,319,333 shares issued and outstanding, as adjusted	66,995	70,133
Retained earnings	10,266	10,266
Accumulated other comprehensive loss	(2,429)	(2,429)
Additional paid-in-capital, warrants	794	794
Total shareholders' equity	75,626	78,764
Total capitalization	\$ 121,940	\$ 125,078

(1)

Does not include (a) 4,498,499 shares of common stock issuable upon the exercise of stock options outstanding as of June 30, 2006 at a weighted average exercise price of \$3.44 per share, (b) 272,000 shares issuable upon exercise of a warrant at an exercise price of \$4.85 per share, (c) 1,657,131 additional shares reserved for future grants or issuances under our stock option plans, (d) 140,483 shares that may be issued upon exercise of the underwriter's overallotment option, and (e) 1,000 shares that Levine Leichtman may acquire upon exercise of a warrant.

(2)

Includes indebtedness outstanding under the renewable subordinated notes program that is due within twelve months after March 31, 2006.

(3)

Does not include (a) securitization trust debt of \$1,100.6 million, (b) indebtedness under warehouse credit facilities of \$75.1 million, and (c) residual interest financing of \$37.7 million, all as of March 31, 2006.

**SELECTED CONSOLIDATED FINANCIAL DATA**

The following table presents our selected consolidated financial data and operating data as of and for the dates indicated. The data under the captions **Statement of Operations Data** and **Balance Sheet Data** have been derived from our audited and unaudited consolidated financial statements. The remainder is derived from other records of ours.

You should read the selected consolidated financial data together with **Capitalization**, **Management's Discussion and Analysis of Financial Condition and Results of Operations** and our audited and unaudited financial statements and notes thereto that are included in this prospectus.

	<b>As of and For the Three Months Ended March 31,</b>		<b>As of and For the Year Ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>
(dollars in thousands, except per share data)					
	(unaudited)				
<b>Statement of Operations Data</b>					
Revenues:					
Interest income	\$ 54,527	\$ 36,172	\$ 171,834	\$ 105,818	\$ 58,164
Servicing fees	1,005	2,264	6,647	12,480	17,058
Net gain on sale of contracts					10,421
Other income	2,492	3,397	15,216	14,394	19,343
Total revenues	58,024	41,833	193,697	132,692	104,986
Expenses:					
Employee costs	9,357	10,450	40,384	38,173	37,141
General and administrative	9,743	8,926	39,285	33,936	31,581
Interest expense	18,035	10,384	51,669	32,147	23,861
Provision for credit losses	19,099	12,312	58,987	32,574	11,390
Impairment loss on residual assets (1)				11,750	4,052
Total expenses	56,234	42,072	190,325	148,580	108,025
Income (loss) before income tax benefit	1,790	(239 )	3,372	(15,888 )	(3,039 )
Income tax benefit					(3,434 )
Net income (loss)	\$ 1,790	\$ (239 )	\$ 3,372	\$ (15,888 )	\$ 395
Earnings (loss) per share basic	\$ 0.08	\$ (0.01 )	\$ 0.16	\$ (0.75 )	\$ 0.02
Earnings (loss) per share diluted	\$ 0.07	\$ (0.01 )	\$ 0.14	\$ (0.75 )	\$ 0.02
Weighted average shares outstanding basic	21,732	21,528	21,627	21,111	20,263
Weighted average shares outstanding diluted	24,188	21,528	23,513	21,111	21,578

**Balance Sheet Data**

Total assets	\$ 1,354,223	\$ 850,533	\$ 1,155,144	\$ 766,599	\$ 492,470
Cash and cash equivalents	25,504	9,730	17,789	14,366	33,209
Restricted cash and equivalents	212,428	150,059	157,662	125,113	67,277
Finance receivables, net	1,050,825	620,302	913,576	550,191	266,189
Residual interest in securitizations	22,608	44,135	25,220	50,430	111,702
Warehouse lines of credit	75,056	50,535	35,350	34,279	33,709
Residual interest financing	37,728	16,411	43,745	22,204	
Securitization trust debt	1,100,606	619,430	924,026	542,815	245,118
Long-term debt	46,314	73,829	58,655	74,829	102,465
Shareholders equity	75,626	69,808	73,589	69,920	82,160

(dollars in thousands, except per share data)	<b>As of and For the Three Months Ended March 31,</b>		<b>As of and For the Year Ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>
	(unaudited)				
<b>Contract Purchases/Securitizations</b>					
Automobile contract purchases	\$ 255,586	\$ 144,165	\$ 691,252	\$ 447,232	\$ 357,320
Automobile contract acquisitions (2)				74,901	152,143
Automobile contracts securitized structured as sales					254,436
Automobile contracts securitized structured as secured financings	245,000	137,390	698,353	491,269	162,488
<b>Managed Portfolio Data</b>					
Contracts held by consolidated subsidiaries	\$ 1,144,340	\$ 691,967	\$ 1,000,597	\$ 619,794	\$ 317,952
Contracts held by non-consolidated subsidiaries	83,162	193,823	103,130	233,621	425,534
SeaWest third party portfolio (3)	12,456	40,501	18,018	53,463	
Total managed portfolio	\$ 1,239,958	\$ 926,291	\$ 1,121,745	\$ 906,878	\$ 743,485
Average managed portfolio	1,191,132	915,547	997,697	861,261	674,523
Weighted average fixed effective interest rate (total managed portfolio) (4)	18.6 %	19.0 %	18.6 %	19.2 %	19.7 %
Core operating expense (% of average managed portfolio) (5)	6.5 %	8.5 %	8.0 %	8.4 %	10.4 %
Allowance for loan losses	\$ 63,846	\$ 46,284	\$ 57,728	\$ 42,615	\$ 35,889
Allowance for loan losses (% of total contracts held by consolidated subsidiaries)	5.6 %	6.7 %	5.8 %	6.9 %	11.3 %
Total delinquencies (% of total managed portfolio) (6)	1.8 %	2.1 %	3.8 %	4.0 %	4.7 %



Total delinquencies and repossessions (% of total managed portfolio)					
(6)	2.7 %	3.2 %	5.0 %	5.6 %	6.2 %
Net charge-offs (% of average managed portfolio) (4)(7)	4.8 %	6.6 %	5.3 %	7.8 %	6.8 %
(1)					

The impairment loss was related to our analysis and estimate of the expected ultimate performance of our previously securitized pools that were held by our non-consolidated subsidiaries and the residual interest in securitizations. The impairment loss was a result of the actual net loss and prepayment rates exceeding our previous estimates for the automobile contracts held by our non-consolidated subsidiaries.

(2)

Represents automobile contracts not purchased directly from dealers, but acquired as a result of our acquisitions of TFC in 2003 and of certain assets of SeaWest in 2004.

(3)

Receivables related to the SeaWest third party portfolio, on which we earn only a servicing fee.

(4)

Excludes receivables related to the SeaWest third party portfolio.

(5)

Total expenses excluding provision for credit losses, interest expense and impairment loss on residual assets.

(6)

For further information regarding delinquencies and the managed portfolio, see the table captioned *Delinquency Experience*, at page 45 of this prospectus and the notes to that table.

(7)

Net charge-offs include the remaining principal balance, after the application of the net proceeds from the liquidation of the vehicle (excluding accrued and unpaid interest) and amounts collected subsequent to the date of the charge-off. For further information regarding charge-offs, see the table captioned *Net Charge-Off Experience*, at page 46 of this prospectus and the notes to that table.

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis should be read in conjunction with our consolidated financial statements and notes thereto and other information included or incorporated by reference herein.

### **Overview**

We are a specialty finance company engaged in purchasing and servicing new and used retail automobile contracts originated primarily by franchised automobile dealerships and to a lesser extent by select independent dealers of used automobiles in the United States. We serve as an alternative source of financing for dealers, facilitating sales to sub-prime customers, who have limited credit history, low income or past credit problems and who otherwise might not be able to obtain financing from traditional sources. We do not currently lend money directly to consumers but, rather, purchase automobile contracts from dealers under several different financing programs. We are headquartered in Irvine, California and have three additional strategically located servicing branches in Virginia, Florida and Illinois.

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

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

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

### **Securitization and Warehouse Credit Facilities**

#### ***Generally***

Throughout the periods for which information is presented in this report, we have purchased automobile contracts with the intention of financing them on a long-term basis through securitizations, and on an interim basis through our warehouse credit facilities. All such financings have involved identification of specific automobile contracts, sale of those automobile contracts (and associated rights) to one of our special-purpose subsidiaries, and issuance of asset-backed securities to fund the transactions. Depending on the structure, these transactions may be accounted for under generally accepted accounting principles as sales of the automobile contracts or as secured financings.

When structured to be treated as a secured financing for accounting purposes, the subsidiary is consolidated with us. Accordingly, the sold automobile contracts and the related debt appear as assets and liabilities, respectively, on our consolidated balance sheet. We then periodically (i) recognize interest and fee income on the contracts, (ii) recognize interest expense on the securities issued in the transaction and (iii) record as expense a provision for credit losses on

the contracts.

When structured to be treated as a sale for accounting purposes, the assets and liabilities of the special-purpose subsidiary are not consolidated with us. Accordingly, the transaction removes the sold automobile contracts from our consolidated balance sheet, the related debt does not appear as our debt, and our consolidated balance sheet shows, as an asset, a retained residual interest in the sold automobile contracts. The residual interest represents the

discounted value of what we expect will be the excess of future collections on the automobile contracts over principal and interest due on the asset-backed securities. That residual interest appears on our consolidated balance sheet as residual interest in securitizations, and the determination of its value is dependent on our estimates of the future performance of the sold automobile contracts.

### ***Change in Policy***

Beginning in the third quarter of 2003, we began to structure our securitization transactions so that they would be treated for financial accounting purposes as secured financings, rather than as sales. All subsequent securitizations of automobile contracts have been so structured. Prior to the third quarter of 2003, we had structured our securitization transactions to be treated as sales of automobile contracts for financial accounting purposes. In our acquisitions of MFN and TFC, we acquired automobile contracts that these companies had previously securitized in securitization transactions that were treated as secured financings for financial accounting purposes. As of March 31, 2006, our consolidated balance sheet included net finance receivables of \$19.0 million and securitization trust debt of \$4.7 million related to automobile contracts acquired in the two mergers, out of totals of net finance receivables of \$1,050.8 million and securitization trust debt of \$1,100.6 million.

### **Credit Risk Retained**

Whether a sale of automobile contracts in connection with a securitization or warehouse credit facility is treated as a secured financing or as a sale for financial accounting purposes, the related special-purpose subsidiary may be unable to release excess cash to us if the credit performance of the related automobile contracts falls short of pre-determined standards. Such releases represent a material portion of the cash that we use to fund our operations. An unexpected deterioration in the performance of such automobile contracts could therefore have a material adverse effect on both our liquidity and our results of operations, regardless of whether such automobile contracts are treated for financial accounting purposes as having been sold or as having been financed. For estimation of the magnitude of such risk, it may be appropriate to look to the size of our managed portfolio, which represents both financed and sold automobile contracts as to which such credit risk is retained. Our managed portfolio as of March 31, 2006 was approximately \$1,240.0 million (this amount includes \$12.5 million of automobile contracts securitized by SeaWest, on which we earn only servicing fees and have no credit risk).

### **Critical Accounting Policies**

We believe that our accounting policies related to (a) Allowance for Finance Credit Losses, (b) Residual Interest in Securitizations and Gain on Sale of Automobile Contracts and (c) Income Taxes are considered to be the most critical to understanding and evaluating our reported financial results. Such policies are described below.

#### ***Allowance for Finance Credit Losses***

In order to estimate an appropriate allowance for losses to be incurred on finance receivables, we use a loss allowance methodology commonly referred to as static pooling, which stratifies our finance receivable portfolio into separately identified pools. Using analytical and formula driven techniques, we estimate an allowance for finance credit losses, which we believe is adequate for probable credit losses that can be reasonably estimated in our portfolio of automobile contracts. Provision for losses is charged to our consolidated statement of operations. Net losses incurred on finance receivables are charged to the allowance. We evaluate the adequacy of the allowance by examining current delinquencies, the characteristics of the portfolio and the value of the underlying collateral. As conditions change, our level of provisioning and/or allowance may change as well.

#### ***Residual Interest in Securitizations and Gain on Sale of Automobile Contracts***

In transactions prior to the third quarter of 2003, we recognized gain on sale on the disposition of automobile contracts either outright, in securitization transactions, and in certain of our warehouse credit facilities. In those securitization transactions and in the warehousing transactions that were treated as sales for financial accounting purposes, we, or one of our wholly-owned, consolidated subsidiaries, retain a residual interest in the automobile contracts that were sold to a wholly-owned, unconsolidated special purpose subsidiary.

The line item residual interest in securitizations on our consolidated balance sheet represents the residual interests in securitizations completed prior to the third quarter of 2003. This line represents the discounted sum of

expected future cash flows from these securitization trusts. Accordingly, the valuation of the residual interest is heavily dependent on estimates of future performance of the automobile contracts included in the securitizations.

We structured all subsequent securitizations and warehouse credit facilities as secured financings. The warehouse credit facilities are accordingly reflected in the line items Finance receivables and Warehouse lines of credit on our consolidated balance sheet, and the securitizations are reflected in the line items Finance receivables and Securitization trust debt.

The key economic assumptions used in measuring all residual interests as of March 31, 2006, December 31, 2005 and December 31, 2004 are included in the table below. We have used an effective pre-tax discount rate of 14% per annum except for certain collections from charged off receivables related to our securitizations executed from 2001 through the second quarter of 2003. With respect to collections from such charged off receivables, we have used a discount rate of 25% per annum.

	3/31/2006		12/31/2005		12/31/2004	
Prepayment speed (cumulative)	22.2%	35.3%	22.2%	35.8%	20.0%	30.5%
Net credit losses (cumulative)	12.3%	20.0%	11.9%	20.2%	13.0%	20.5%

Key economic assumptions and the sensitivity of the fair value of residual cash flows to immediate 10% and 20% adverse changes in those assumptions as of December 2005 are as follows:

	December 31, 2005	
(dollars in thousands)		
Carrying amount/fair value of residual interest in securitizations		\$25,220
Weighted average life in years		2.24
Prepayment speed assumption (cumulative)	22.2%	35.8%
Estimated fair value assuming 10% adverse change		\$25,168
Estimated fair value assuming 20% adverse change		25,119
Expected net credit losses (cumulative)	11.9%	20.2%
Estimated fair value assuming 10% adverse change		\$23,937
Estimated fair value assuming 20% adverse change		22,656
Residual cash flows discount rate (annual)	14.0%	25.0%
Estimated fair value assuming 10% adverse change		\$24,636
Estimated fair value assuming 20% adverse change		24,071

These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in fair value based on 10% and 20% variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, in this table, the effect of a variation in a particular assumption on the fair value of the retained interest is calculated without changing any other assumption; in reality, changes in one factor may result in changes in another (for example, increases in market rates may result in lower prepayments and increased credit losses), which could magnify or counteract the sensitivities.

Our term securitization structure has generally been as follows:

We sell automobile contracts we acquire to a wholly-owned special purpose subsidiary, which has been established for the limited purpose of buying and reselling our automobile contracts. The special-purpose subsidiary then transfers the same automobile contracts to another entity, typically a statutory trust. The trust issues interest-bearing asset-backed securities, in a principal amount equal to or less than the aggregate principal balance of the automobile contracts. We typically sell these automobile contracts to the trust at face value and without recourse, except that representations and warranties similar to those provided by the dealer to us are provided by us to the trust. One or more investors purchase the asset-backed securities issued by the trust; the proceeds from the sale of the asset-backed securities are then used to purchase the automobile contracts from us. We may retain or sell subordinated asset-backed securities issued by the trust or by a related entity. We purchase external credit enhancement in the form of a financial guaranty insurance policy, guaranteeing timely payment of principal and interest on the senior asset-backed securities, from an insurance company. In addition, we structure our

securitizations to include internal credit enhancement for the benefit of the insurance company and the investors (i) in the form of an initial cash deposit to an account ( spread account ) held by the trust, (ii) in the form of overcollateralization of the senior asset-backed securities, where the principal balance of the senior asset-backed securities issued is less than the principal balance of the automobile contracts, (iii) in the form of subordinated asset-backed securities, or (iv) some combination of such internal credit enhancements. The agreements governing the securitization transactions require that the initial level of internal credit enhancement be supplemented by a portion of collections from the automobile contracts until the level of internal credit enhancement reaches specified levels, which are then maintained. The specified levels are generally computed as a percentage of the principal amount remaining unpaid under the related automobile contracts. The specified levels at which the internal credit enhancement is to be maintained will vary depending on the performance of the portfolios of automobile contracts held by the trusts and on other conditions, and may also be varied by agreement among us, our special purpose subsidiary, the insurance company and the trustee. Such levels have increased and decreased from time to time based on performance of the various portfolios, and have also varied from one transaction to another. The agreements governing the securitizations generally grant us the option to repurchase the sold automobile contracts from the trust when the aggregate outstanding balance of the automobile contracts has amortized to a specified percentage of the initial aggregate balance.

The prior securitizations that were treated as sales for financial accounting purposes differ from those treated as secured financings in that the trust to which our special-purpose subsidiaries sold the automobile contracts met the definition of a qualified special-purpose entity under Statement of Financial Accounting Standards No. 140 ( SFAS 140 ). As a result, assets and liabilities of those trusts are not consolidated into our consolidated balance sheet.

Our warehouse credit facility structures are similar to the above, except that (i) our special-purpose subsidiaries that purchase the automobile contracts pledge the automobile contracts to secure promissory notes that they issue, (ii) the promissory notes are in an aggregate principal amount of not more than 80.0% of the aggregate principal balance of the automobile contracts (that is, at least 20.0% overcollateralization), (iii) no increase in the required amount of internal credit enhancement is contemplated unless certain portfolio performance tests are breached, and (iv) we do not purchase financial guaranty insurance. During the third quarter of 2003, we agreed with our warehouse lenders to amend the agreements governing our warehouse credit facilities. The effect of these amendments was to cause the transactions to be treated as secured financings for financial accounting purposes.

Upon each sale of automobile contracts in a transaction structured as a secured financing for financial accounting purposes, whether a term securitization or a warehouse financing, we retain on our consolidated balance sheet the related automobile contracts as assets and record the asset-backed notes issued in the transaction as indebtedness.

Under the prior securitizations and warehouse credit facilities structured as sales for financial accounting purposes, we removed from our consolidated balance sheet the automobile contracts sold and added to our consolidated balance sheet (i) the cash received, if any, and (ii) the estimated fair value of the ownership interest that we retained in the automobile contracts sold in the transaction. That retained or residual interest consisted of (a) the cash held in the spread account, if any, (b) overcollateralization, if any, (c) subordinated asset-backed securities retained, if any, and (d) receivables from trust, which include the net interest receivables. Net interest receivables represent the estimated discounted cash flows to be received from the trust in the future, net of principal and interest payable with respect to the asset-backed notes, and certain expenses. The excess of the cash received and the assets we retained over the carrying value of the automobile contracts sold, less transaction costs, equaled the net gain on sale of automobile contracts we recorded. Until the maturity of these transactions, our consolidated balance sheet will reflect both securitization transactions structured as sales and others structured as secured financings.

With respect to transactions structured as sales for financial accounting purposes, we allocate our basis in the automobile contracts between the asset-backed securities sold and the residual interests retained based on the relative fair values of those portions on the date of the sale. We recognize gains or losses attributable to the change in the fair value of the residual interests, which are recorded at estimated fair value. We are not aware of an active market for the



purchase or sale of interests such as the residual interests; accordingly, we determine the estimated fair value of the residual interests by discounting the amount of anticipated cash flows that we estimate will be released to us in the future (the cash out method), using a discount rate that we believe is appropriate for the risks involved. The anticipated cash flows include collections from both current and charged off receivables. We have used an effective pre-tax discount rate of 14% per annum, except for certain collections from charged off receivables

related to our securitizations executed from 2001 through the second quarter of 2003. With respect to collections from such charged off receivables, we have used a discount rate of 25% per annum.

We receive periodic base servicing fees for the servicing and collection of the automobile contracts. (Under our current securitization structure, such servicing fees are included in interest income from the automobile contracts). In addition, we are entitled to the cash flows from the trusts that represent collections on the automobile contracts in excess of the amounts required to pay principal and interest on the asset-backed securities, the base servicing fees, and certain other fees and expenses (such as trustee and custodial fees). Required principal payments on the notes are generally defined as the payments sufficient to keep the principal balance of such notes equal to the aggregate principal balance of the related automobile contracts (excluding those automobile contracts that have been charged off), or a pre-determined percentage of such balance. Where that percentage is less than 100%, the related securitization agreements require accelerated payment of principal until the principal balance of the asset-backed securities is reduced to the specified percentage. Such accelerated principal payment is said to create overcollateralization of the asset-backed notes.

If the amount of cash required for payment of fees, expenses, interest and principal exceeds the amount collected during the collection period, the shortfall is withdrawn from the spread account, if any. If the cash collected during the period exceeds the amount necessary for the above allocations, and there is no shortfall in the related spread account or the required overcollateralization level, the excess is released to us, or in certain cases is transferred to other spread accounts related to transactions that may be below their required levels. If the spread account and overcollateralization is not at the required level, then the excess cash collected is retained in the trust until the specified level is achieved. Although spread account balances are held by the trusts on behalf of our special-purpose subsidiaries as the owner of the residual interests (in the case of securitization transactions structured as sales for financial accounting purposes) or the trusts (in the case of securitization transactions structured as secured financings for financial accounting purposes), we are restricted in use of the cash in the spread accounts. Cash held in the various spread accounts is invested in high quality, liquid investment securities, as specified in the securitization agreements. The interest rate payable on the automobile contracts is significantly greater than the interest rate on the asset-backed notes. As a result, the residual interests described above are a significant asset of ours. In determining the value of the residual interests, we must estimate the future rates of prepayments, delinquencies, defaults, default loss severity, and recovery rates, as all of these factors affect the amount and timing of the estimated cash flows. We estimate prepayments by evaluating historical prepayment performance of comparable automobile contracts. We estimate recovery rates of previously charged off receivables using available historical recovery data. We estimate defaults and default loss severity using available historical loss data for comparable automobile contracts and the specific characteristics of the automobile contracts we purchased. In valuing the residuals as of March 31, 2006, we estimate that charge-offs as a percentage of the original principal balance will approximate 16.5% to 25.9% cumulatively over the lives of the related automobile contracts, with recovery rates approximating 4.3% to 5.9% of the original principal balance and prepayment estimates of approximately 22.2% to 35.3% cumulatively over the lives of the related automobile contracts.

For securitizations that were structured as a sale for financial accounting purposes, we recognize interest income on the balance of the residual interests. In addition, we would recognize as gain additional revenue from the residual interests if the actual performance of the automobile contracts were better than our estimate of the value of the residual interest. If the actual performance of the automobile contracts were worse than our estimate, then a downward adjustment to the carrying value of the residuals and a related impairment charge would be required. In a securitization structured as a secured financing for financial accounting purposes, interest income is recognized when accrued under the terms of the related automobile contracts and, therefore, presents less potential for fluctuations in performance when compared to the approach used in a transaction structured as a sale for financial accounting purposes.

In all of our term securitizations and warehouse credit facilities, whether treated as secured financings or as sales, we have sold the automobile contracts (through a subsidiary) to the securitization trust. The difference between the two structures is that in securitizations that are treated as secured financings we report the assets and liabilities of the

securitization trust on our consolidated balance sheet. Under both structures, recourse to us by holders of the asset-backed securities and by the trust, for failure of the automobile contract obligors to make payments on a timely basis, is limited to the automobile contracts included in the securitizations or warehouse credit facilities, the spread accounts and our residual interests in the respective trusts.

### ***Income Taxes***

We and our subsidiaries file a consolidated federal income tax return and combined or stand-alone state franchise tax returns for certain states. We utilize the asset and liability method of accounting for income taxes, under which deferred income taxes are recognized for the future tax consequences attributable to the differences between the financial statement values of existing assets and liabilities and their respective tax bases. We measure deferred tax assets and liabilities using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date. We have estimated a valuation allowance against that portion of the deferred tax asset whose utilization in future periods is not more than likely.

In determining the possible realization of deferred tax assets, we consider future taxable income from the following sources: (a) the reversal of taxable temporary differences; (b) future operations exclusive of reversing temporary differences; and (c) tax planning strategies that, if necessary, would be implemented to accelerate taxable income into periods in which net operating losses might otherwise expire.

See *Liquidity and Capital Resources* and Note 1 of Notes to Consolidated Financial Statements.

### **Results of Operations**

#### ***Effects of Change in Securitization Structure***

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

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

Since the third quarter of 2003, we have conducted sixteen term securitizations. Of these sixteen, twelve were quarterly securitizations of automobile contracts that we purchased from automobile dealers under our regular programs. In addition, in March 2004 and November 2005, we completed securitizations of our retained interests in other securitizations that we and our affiliates previously sponsored. The debt from the March 2004 transaction was repaid in August 2005. Also, in June 2004, we completed a securitization of automobile contracts purchased in the SeaWest asset acquisition and under our TFC programs. Further, in December 2005, we completed a securitization that included automobile contracts purchased under the TFC programs, automobile contracts purchased under the CPS programs and automobile contracts we repurchased upon termination of prior securitizations of our MFN and TFC

subsidiaries. All such securitizations since the third quarter of 2003 have been structured as secured financings.

***Comparison of Operating Results for the Three Months Ended March 31, 2006 with the Three Months Ended March 31, 2005***

*Revenues.* During the three months ended March 31, 2006, revenues were \$58.0 million, an increase of \$16.2 million, or 38.7%, from the prior year period revenue of \$41.8 million. The primary reason for the increase in revenues is an increase in interest income. Interest income for the three months ended March 31, 2006 increased

\$18.4 million, or 50.7%, to \$54.5 million from \$36.2 million in the prior year period. The primary reason for the increase in interest income is the increase in finance receivables held by consolidated subsidiaries (resulting in an increase of \$22.5 million in interest income). This increase was partially offset by the decline in the balance of the portfolios of automobile contracts we acquired in the MFN, TFC and SeaWest transactions (in the aggregate, resulting in a decrease of \$3.4 million in interest income), and a decrease of \$723,000 in interest earned on our residual asset.

Servicing fees totaling \$1.0 million in the three months ended March 31, 2006 decreased \$1.3 million, or 55.6%, from \$2.3 million in the same period a year earlier. The decrease in servicing fees is the result of the change in securitization structure and the consequent decline in our managed portfolio held by non-consolidated subsidiaries. As a result of the decision to structure future securitizations as secured financings, our managed portfolio held by non-consolidated subsidiaries will continue to decline in future periods, and servicing fee revenue is anticipated to decline proportionately. As of March 31, 2006 and 2005, our managed portfolio owned by consolidated vs. non-consolidated subsidiaries and other third parties was as follows:

(dollars in millions)	March 31, 2006		March 31, 2005	
	Amount	%	Amount	%
<b>Total managed portfolio</b>				
Owned by consolidated subsidiaries	\$ 1,144.3	92.3 %	\$ 692.0	74.7 %
Owned by non-consolidated subsidiaries	83.2	6.7	193.8	20.9
SeaWest third party portfolio	12.5	1.0	40.5	4.4
Total	\$ 1,240.0	100.0 %	\$ 926.3	100.0 %

At March 31, 2006, we were generating income and fees on a managed portfolio with an outstanding principal balance of \$1,240.0 million (this amount includes \$12.5 million of automobile contracts securitized by SeaWest, on which we earn only servicing fees), compared to a managed portfolio with an outstanding principal balance of \$926.3 million as of March 31, 2005. As the portfolios of automobile contracts acquired in the MFN, TFC Merger and SeaWest transactions decrease, the portfolio of automobile contracts that we purchased directly from automobile dealers continues to expand. At March 31, 2006 and 2005, the managed portfolio composition was as follows:

(dollars in millions)	March 31, 2006		March 31, 2005	
	Amount	%	Amount	%
<b>Originating Entity</b>				
CPS	\$ 1,150.5	92.8 %	\$ 760.1	82.1 %
TFC	64.7	5.2	83.5	9.0
MFN	1.3	0.1	11.1	1.2
SeaWest	11.0	0.9	31.1	3.4
SeaWest third party portfolio	12.5	1.0	40.5	4.4
Total	\$ 1,240.0	100.0 %	\$ 926.3	100.0 %

Other income decreased \$904,000, or 26.6%, to \$2.5 million in the three-month period ended March 31, 2006 from \$3.4 million during the same period a year earlier. The period over period decrease resulted primarily from decreases in recoveries on MFN and certain other automobile contracts (a decrease of \$792,000) compared to the same period of the prior year and decreased revenue on our direct mail services (a decrease of \$340,000). These direct mail services are provided to our dealers and consist of customized solicitations targeted to prospective vehicle purchasers, in proximity to the dealer, who appear to meet our credit criteria. Decreases in other income for the period were somewhat offset by increases in convenience fees charged to obligors for certain transaction types (an increase of \$228,000).

*Expenses.* Our operating expenses consist primarily of provisions for credit losses, interest expense, employee costs and general and administrative expenses. Provisions for credit losses and interest expense are significantly affected by the volume of automobile contracts we purchased during a period and by the outstanding balance of finance receivables held by consolidated subsidiaries. Employee costs and general and administrative expenses are incurred as applications and automobile contracts are received, processed and serviced. Factors that affect margins and net income include changes in the automobile and automobile finance market environments, and macroeconomic factors such as interest rates and the unemployment level.

Employee costs include base salaries, commissions and bonuses paid to employees, and certain expenses related to the accounting treatment of outstanding warrants and stock options, and are one of our most significant operating expenses. These costs (other than those relating to stock options) generally fluctuate with the level of applications and automobile contracts processed and serviced.

Other operating expenses consist primarily of facilities expenses, telephone and other communication services, credit services, computer services (including employee costs associated with information technology support), professional services, marketing and advertising expenses, and depreciation and amortization.

Total operating expenses were \$56.2 million for the three months ended March 31, 2006, compared to \$42.1 million for the same period a year earlier, an increase of \$14.2 million, or 33.7%. The increase is primarily due to increases in provision for credit losses and interest expense, which increased by \$6.8 million and \$7.7 million, or 55.1% and 73.7% respectively. Both interest expense and provision for credit losses are directly affected by the growth in our portfolio of automobile contracts held by consolidated affiliates.

Employee costs decreased slightly to \$9.4 million during the three months ended March 31, 2006, representing 16.6 % of total operating expenses, from \$10.5 million for the same period a year earlier, or 24.8% of total operating expenses. During the period ended March 31, 2006, we deferred \$946,000 of direct employee costs associated with the purchase of automobile contracts in the period, in accordance with Statement of Financial Accounting Standard No. 91, Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases (SFAS 91). Historically, we have not deferred and amortized such costs as our analyses indicated that the effect of such deferral and amortization would not have been material. However, due to continued increases in volumes of automobile contract purchases and refinements in our methodology to measure direct costs associated with automobile contract purchases, our estimate of direct costs has increased, resulting in the need to defer such costs and amortize them over the lives of the related automobile contracts as an adjustment to the yield in accordance with SFAS 91. The decrease as a percentage of total operating expenses reflects the higher total of operating expenses, primarily a result of the increased provision for credit losses and interest expense.

General and administrative expenses decreased slightly by \$27,000 or 0.5% and represented 9.1% of total operating expenses in the three-month period ending March 31, 2006, as compared to the prior year period when general and administrative expenses represented 12.2% of total operating expenses. The decrease as a percentage of total operating expenses reflects the higher operating expenses primarily a result of the provision for credit losses and interest expense.

Interest expense for the three-month period ended March 31, 2006 increased \$7.7 million, or 73.7%, to \$18.0 million, compared to \$10.4 million in the same period of the previous year. The increase is primarily the result of changes in the amount and composition of securitization trust debt carried on our consolidated balance sheet. Such debt increased as a result of the change in securitization structure implemented in the third quarter of 2003 (resulting in an increase of \$8.9 million in interest expense), partially offset by the decrease in the balance of the securitization trust debt acquired in the MFN and TFC transaction (resulting in a decrease of \$309,000 in interest expense) and a decrease in interest expense on certain long-term debt (a decrease of \$870,000).

Marketing expenses increased by \$737,000, or 26.3%, to \$3.5 million, compared to \$2.8 million in the same period of the previous year and represented 6.3% of total operating expenses. The increase is primarily due to the increase in automobile contracts we purchased during the three months ended March 31, 2006 as compared to the prior year period. During the period ended March 31, 2006, we purchased 16,953 automobile contracts aggregating \$255.6 million, compared to 10,103 automobile contracts aggregating \$144.2 million in the same period of the prior year.

Occupancy expenses increased by \$121,000, or 15.5%, to \$903,000 compared to \$782,000 in the same period of the previous year and represented 1.6% of total operating expenses.



Depreciation and amortization expenses decreased by \$14,000, or 6.8%, to \$193,000 from \$207,000 in the same period of the previous year.

**Comparison of Operating Results For The Year Ended December 31, 2005 With the Year Ended December 31, 2004**

*Revenues.* During the year ended December 31, 2005, revenues were \$193.7 million, an increase of \$61.0 million, or 46.0%, from the prior year revenue of \$132.7 million. The primary reason for the increase in revenues is an increase in interest income. Interest income for the year ended December 31, 2005 increased \$66.0 million, or 62.4%, to \$171.8 million in 2005 from \$105.8 million in 2004. The primary reason for the increase in interest income is the growth of the finance receivables held by consolidated subsidiaries on our balance sheet. During 2005, we purchased \$691.3 million of automobile contracts and increased our balance of receivables held by consolidated subsidiaries to \$1,000.6 million at December 31, 2005 from \$619.8 million at December 31, 2004, an increase of 61.4%. Offsetting the increase in interest income were decreases in the balance of receivables acquired in the MFN, TFC and SeaWest transactions, which resulted in decreases in interest income of \$1.8 million, \$2.0 million and \$2.6 million, respectively.

Servicing fees totaling \$6.6 million in the year ended December 31, 2005 decreased \$5.8 million, or 46.7%, from \$12.5 million in the same period a year earlier. The decrease in servicing fees is the result of the change in securitization structure and the consequent decline in our managed portfolio held by non-consolidated subsidiaries, and the decrease in the balance of automobile contracts originated by SeaWest for which we receive only servicing fees. As a result of the decision to structure future securitizations as secured financings, our managed portfolio held by non-consolidated subsidiaries will continue to decline in future periods, and servicing fee revenue is anticipated to decline proportionately. As of December 31, 2005 and 2004, our managed portfolio owned by consolidated vs. non-consolidated subsidiaries and other third parties was as follows:

(dollars in millions)	December 31, 2005		December 31, 2004	
	Amount	%	Amount	%
<b>Total managed portfolio</b>				
Owned by consolidated subsidiaries	\$ 1,000.6	89.2 %	\$ 619.8	68.3 %
Owned by non-consolidated subsidiaries	103.1	9.2	233.6	25.8
SeaWest third party portfolio	18.0	1.6	53.5	5.9
Total	\$ 1,121.7	100.0 %	\$ 906.9	100.0 %

At December 31, 2005, we were generating income and fees on a managed portfolio with an outstanding principal balance of \$1,121.7 million (this amount includes \$18.0 million of automobile contracts securitized by SeaWest, on which we earn only servicing fees), compared to a managed portfolio with an outstanding principal balance of \$906.9 million as of December 31, 2004. As the portfolios of automobile contracts acquired in the MFN, TFC and SeaWest transactions decrease, the portfolio of automobile contracts that we purchased directly from automobile dealers continues to expand. At December 31, 2005 and 2004, the managed portfolio composition was as follows:

(dollars in millions)	December 31, 2005		December 31, 2004	
	Amount	%	Amount	%
<b>Originating Entity</b>				
CPS	\$ 1,017.3	90.7 %	\$ 706.8	77.9 %
TFC	68.6	6.1	89.4	9.9
MFN	2.5	0.1	17.8	2.0
SeaWest	15.3	1.4	39.4	4.3
SeaWest third party portfolio	18.0	1.6	53.5	5.9
Total	\$ 1,121.7	100.0 %	\$ 906.9	100.0 %

Other income increased \$822,000, or 5.7%, to \$15.2 million during 2005 from \$14.4 million in 2004. During 2005, other income included \$2.4 million from the sale of charged off receivables acquired in the MFN, TFC, and SeaWest transactions, compared to no such proceeds in 2004. Recoveries on MFN receivables decreased by \$3.1 million to \$4.9 million in 2005, compared to \$8.0 million in 2004. Other income associated with direct mail services increased by \$765,000 to \$4.5 million in 2005, compared to \$3.8 million in 2004. These direct mail services are provided to our dealers and represent direct mail products which consist of customized solicitations targeted to prospective vehicle purchasers, in proximity to the Dealer, who are likely to meet our credit criteria.

*Expenses.* Total operating expenses were \$190.3 million for 2005, compared to \$148.6 million for 2004. The increase is primarily due to a \$26.4 million increase, or 81.1% in the provision for credit losses to \$59.0 million during the 2005 period as compared to \$32.6 million in the 2004 period. Interest expense increased by \$19.5 million to \$51.7 million from \$32.1 million in 2004, an increase of 60.7%. The increase is primarily the result of the amount of securitization trust debt carried on our consolidated balance sheet, which increased along with the growth of our portfolio of finance receivables. The increase was somewhat offset by the decrease in securitization trust debt acquired in the MFN and TFC transactions. For 2005, the provision for credit losses and interest expense represented 31.0% and 27.1%, respectively, of total operating expenses, compared to 21.9% and 21.6% in 2004.

Employee costs increased to \$40.4 million, or 5.8% during 2005, representing 21.2% of total operating expenses, from \$38.2 million for 2004, or 25.7% of total operating expenses. The decrease as a percentage of total operating expenses reflects the higher total of operating expenses, primarily a result of the increased provision for credit losses and interest expense.

General and administrative expenses increased slightly to \$23.1 million, or 12.1% of total operating expenses, in 2005, as compared to \$21.3 million, or 14.3% of total operating expenses, in 2004. The decrease as a percentage of total operating expenses reflects the higher operating expenses primarily a result of the increased provision for credit losses and interest expense. During the year ended December 31, 2005, we recognized what we believe will be a one-time, non-cash impairment charge of \$1.9 million against certain assets other than finance receivables.

In December 2005, the Compensation Committee of the Board of Directors approved accelerated vesting of all the outstanding stock options we issued. Options to purchase 2,113,998 shares of our common stock, which would otherwise have vested from time to time through 2010, became immediately exercisable as a result of the acceleration of vesting. The decision to accelerate the vesting of the options was made primarily to reduce non-cash compensation expenses that would have been recorded in our income statement in future periods upon the adoption of Financial Accounting Standards Board Statement No. 123R, Share-Based Payment, in January 2006. We estimate that approximately \$3.5 million of future non-cash compensation expense was eliminated as a result of the acceleration of vesting.

At the time of the acceleration of vesting, we accounted for our stock options in accordance with Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees. Consequently, the acceleration of vesting resulted in non-cash compensation charge of \$427,000 for the year ended December 31, 2005.

For 2005, we recognized no impairment loss on our residual interest in securitizations compared to \$11.8 million in 2004. In 2004, such impairment loss related to our analysis and estimate of the expected ultimate performance of our previously securitized pools that are held by non-consolidated subsidiaries and the residual interest in securitizations. The impairment loss was a result of the actual net loss and prepayment rates exceeding our previous estimates for the automobile contracts held by non-consolidated subsidiaries.

Marketing expenses increased by \$3.7 million, or 43.9%, to \$12.0 million, compared to \$8.3 million in the same period of the previous year and represented 6.3% of total operating expenses. The increase is primarily due to the increase in automobile contracts we purchased during the year ended December 31, 2005.

Occupancy expenses decreased by \$120,000, or 3.4%, to \$3.4 million, compared to \$3.5 million in the same period of the previous year and represented 1.8% of total operating expenses. The decrease is primarily due to the closure and sub-leasing during 2005 of certain facilities acquired in the MFN and TFC transactions.

Depreciation and amortization expenses remained essentially unchanged at \$790,000 for 2005, compared to \$785,000 for 2004, and represented 0.4% of total operating expenses.

We would have recorded income tax expense of \$1.4 million for the year ended December 31, 2005, but the income tax expense was offset primarily by a \$1.4 million decrease in the valuation allowance that has been established to offset our deferred tax assets.

***Comparison of Operating Results for the Year Ended December 31, 2004 with the Year Ended December 31, 2003***

*Revenues.* During the year ended December 31, 2004, revenues were \$132.7 million, an increase of \$27.7 million, or 26.4%, from the prior year revenue of \$105.0 million. The primary reason for the increase in revenues is an increase in interest income. Interest income for the year ended December 31, 2004 increased \$47.7 million, or

81.9%, to \$105.8 million in 2004 from \$58.2 million in 2003. The primary reasons for the increase in interest income are the change in securitization structure implemented during the third quarter of 2003 (an increase of \$56.0 million) and the interest income earned on the portfolios of automobile contracts acquired in the TFC transaction (an increase of \$7.2 million) and the SeaWest asset acquisition (an increase of \$6.1 million). This increase was partially offset by the decline in the balance of the portfolio of automobile contracts acquired in the MFN transaction (resulting in a decrease of \$10.1 million in interest income) and a decrease in residual interest income (a decrease of \$11.6 million).

The increase in interest income is offset in part by the elimination of net gain on sale of automobile contracts revenue and a decrease in servicing fees. As a result of the change in securitization structure, no net gain on sale of automobile contracts was recorded in 2004, compared to \$10.4 million net gain on sale in the year earlier period.

Servicing fees totaling \$12.5 million in the year ended December 31, 2004 decreased \$4.6 million, or 26.8%, from \$17.1 million in the same period a year earlier. The decrease in servicing fees is the result of the change in securitization structure and the consequent decline in our managed portfolio held by non-consolidated subsidiaries. The decrease was partially offset by the servicing fees earned on the automobile contracts securitized by SeaWest, on which we earn only a servicing fee, which totaled \$2.0 million. As a result of the decision to structure future securitizations as secured financings, our managed portfolio held by non-consolidated subsidiaries will continue to decline in future periods, and servicing fee revenue is anticipated to decline proportionately. As of December 31, 2004 and 2003, our managed portfolio owned by consolidated vs. non-consolidated subsidiaries and other third parties was as follows:

(dollars in millions)	December 31, 2004		December 31, 2003	
	Amount	%	Amount	%
<b>Total managed portfolio</b>				
Owned by consolidated subsidiaries	\$ 619.8	68.3 %	\$ 318.0	42.8 %
Owned by non-consolidated subsidiaries	233.6	25.8	425.5	57.2
SeaWest third party portfolio	53.5	5.9		0.0
Total	\$ 906.9	100.0 %	\$ 743.5	100.0 %

At December 31, 2004, we were generating income and fees on a managed portfolio with an outstanding principal balance of \$906.9 million (this amount includes \$53.5 million related to automobile contracts securitized by SeaWest, on which we earn only a servicing fee), compared to a managed portfolio with an outstanding principal balance of \$743.5 million as of December 31, 2003. As the portfolios of automobile contracts acquired in the MFN and the TFC transactions decrease, the portfolio of automobile contracts that we purchased directly from automobile dealers continues to expand. At December 31, 2004 and 2003, the managed portfolio composition was as follows:

(dollars in millions)	December 31, 2004		December 31, 2003	
	Amount	%	Amount	%
<b>Originating Entity</b>				
CPS	\$ 706.8	77.9 %	\$ 543.8	73.1 %
TFC	89.4	9.9	126.0	17.0
MFN	17.8	2.0	73.7	9.9
SeaWest	39.4	4.3		0.0
SeaWest third party portfolio	53.5	5.9		0.0
Total	\$ 906.9	100.0 %	\$ 743.5	100.0 %

Other income decreased \$4.9 million, or 25.6%, to \$14.4 million during 2004 from \$19.3 million during 2003. The period over period decrease resulted primarily from a sales tax refund of \$3.0 million received in 2003 and decreased recoveries on previously charged off MFN automobile contracts, which were \$8.0 million during 2004, compared to

\$12.2 million for 2003.

*Expenses.* Total operating expenses were \$148.6 million for 2004, compared to \$108.0 million for 2003. The increase is primarily due to a \$21.2 million increase in the provision for credit losses to \$32.6 million during the 2004 period as compared to \$11.4 million in the 2003 period. Increased interest expense was also significant.

Employee costs increased to \$38.2 million during 2004, representing 25.7% of total operating expenses, from \$37.1 million for 2003, or 34.4% of total operating expenses. The slight increase is primarily the result of staff

additions related to increased automobile contract purchases in 2004 (an increase of \$3.9 million). This increase was partially offset by staff reductions since the MFN transaction in 2002 related to the integration and consolidation of certain service and administrative activities and the decline in the balance of the portfolio of automobile contracts acquired in the MFN transaction (a decrease of \$3.2 million). The decrease as a percentage of total operating expenses reflects the higher total of operating expenses, primarily a result of the increased provision for credit losses and interest expense.

General and administrative expenses remained essentially unchanged at \$21.3 million, or 14.3% of total operating expenses, in 2004, as compared to \$21.3 million, or 19.7% of total operating expenses, in 2003. The decrease as a percentage of total operating expenses reflects the higher operating expenses primarily a result of the provision for credit losses and interest expense.

Interest expense for 2004 increased \$8.3 million, or 34.7%, to \$32.1 million, compared to \$23.9 million in 2003. The increase is primarily the result of changes in the amount and composition of securitization trust debt carried on our consolidated balance sheet. Such debt increased as a result of the change in securitization structure implemented in the third quarter of 2003, the TFC acquisition in May 2003 and the SeaWest asset acquisition in April 2004 (a combined increase in interest expense of approximately \$10.3 million), partially offset by the decrease in the balance of the securitization trust debt acquired in the MFN transaction (resulting in a decrease of approximately \$2.0 million in interest expense).

Impairment loss increased by \$7.7 million, or 190.0%, to \$11.8 million in 2004 as compared to \$4.1 million in 2003. Such impairment loss relates to our analysis and estimate of the expected ultimate performance of our previously securitized pools that are held by non-consolidated subsidiaries and the residual interest in securitizations. The impairment loss is a result of the actual net loss and prepayment rates exceeding our previous estimates for the automobile contracts held by non-consolidated subsidiaries.

Marketing expenses increased by \$3.0 million, or 55.0%, and represented 5.6% of total operating expenses. The increase is primarily due to the increase in automobile contracts we purchased during the year ended December 31, 2004.

Occupancy expenses decreased by \$410,000, or 10.4%, and represented 2.4% of total operating expenses. The decrease is primarily due to the closure and sub-leasing during 2004 of certain facilities acquired in the MFN and TFC transactions.

Depreciation and amortization expenses decreased by \$215,000, or 21.5%, to \$785,000 from \$1.0 million.

No income tax benefit was recorded in 2004 as compared to \$3.4 million recorded in 2003. The 2003 benefit is primarily the result of the resolution of certain Internal Revenue Service examinations of previously filed MFN tax returns, resulting in a tax benefit of \$4.9 million, and other state tax matters resulting in a tax provision of \$1.5 million. We do not expect any comparable income tax benefit in future periods.

## **Liquidity and Capital Resources**

### ***Liquidity***

Our business requires substantial cash to support purchases of automobile contracts and other operating activities. Our primary sources of cash have been cash flows from operating activities, including proceeds from sales of automobile contracts, amounts borrowed under various revolving credit facilities (also sometimes known as warehouse credit facilities), servicing fees on portfolios of automobile contracts previously sold in securitization transactions or serviced for third parties, customer payments of principal and interest on finance receivables, fees for origination of automobile contracts, and releases of cash from securitized portfolios of automobile contracts in which we have



retained a residual ownership interest and from the spread accounts associated with such pools. Our primary uses of cash have been the purchases of automobile contracts, repayment of amounts borrowed under lines of credit and otherwise, operating expenses such as employee, interest, occupancy expenses and other general and administrative expenses, the establishment of spread accounts and initial overcollateralization, if any, and the increase of credit enhancement to required levels in securitization transactions, and income taxes. There can be no assurance that internally generated cash will be sufficient to meet our cash demands. The sufficiency of internally generated cash will depend on the performance of securitized pools (which determines the level of releases from

those portfolios and their related spread accounts), the rate of expansion or contraction in our managed portfolio, and the terms upon which we are able to purchase, sell, and borrow against automobile contracts.

Net cash provided by operating activities for the years ended December 31, 2005, 2004 and 2003 was \$36.7 million, \$10.0 million and \$98.9 million, respectively. Cash from operating activities is generally provided by the net releases from our securitization trusts. The increase in 2005 vs. 2004 is due in part to our increased net earnings before the significant increase in the provision for credit losses. The decrease in 2004 vs. 2003 is primarily the result of our decision, in the third quarter of 2003, to treat all of our future securitizations as secured financings. As a result, 2005 and 2004 include no activity related to automobile contracts held for sale.

Net cash used in operating activities for the three-month period ended March 31, 2006 was \$33.5 million compared to net cash used in operating activities for the three-month period ended March 31, 2005 of \$9.2 million. Cash used in operating activities is affected by the increase in restricted cash as a result of our pre-funding structure used in the securitization of our finance receivables. The pre-funding structure allows us to issue securitization debt approximately one month prior to purchasing finance receivables that collateralize the debt. In those cases, certain of the proceeds of the securitization debt are held as restricted cash until such time as the additional collateral is delivered to the related trust. Increases in restricted cash are offset somewhat by our increased net earnings before the significant increase in the provision for credit losses.

Net cash used in investing activities for the years ended December 31, 2005, 2004 and 2003, was \$411.7 million, \$314.1 million, and \$178.9 million, respectively. Cash used in investing activities has generally related to purchases of automobile contracts, the cost of the SeaWest asset acquisition and the acquisition of TFC. Purchase of finance receivables held for investment were \$691.3 million, \$506.0 million and \$175.3 million in 2005, 2004 and 2003, respectively. Cash used in the TFC acquisition, net of the cash acquired in the transaction, totaled \$10.2 million for the year ended December 31, 2003.

Net cash used in investing activities for the three-month periods ended March 31, 2006 and 2005 was \$153.8 million and \$79.8 million, respectively. Cash used in investing activities has generally related to purchases of automobile contracts.

Net cash provided by financing activities for the year ended December 31, 2005, was \$378.4 million compared with \$285.3 million for the year ended December 31, 2004 and \$80.3 million for the year ended December 31, 2003. Cash used or provided by financing activities is primarily attributable to the issuance or repayment of debt. In connection with the TFC acquisition, we assumed securitization trust debt related to three securitization transactions held by consolidated subsidiaries and assumed additional subordinated debt. With the change in the securitization structure implemented in the third quarter of 2003, \$662.4 million of securitization trust debt was issued in 2005 as compared to \$474.7 million in 2004 and \$154.4 million in 2003.

Net cash provided by financing activities for the three months ended March 31, 2006 and 2005, was \$195.1 million and \$84.4 million respectively. Cash provided by financing activities is generally related to the issuance of new securitization trust debt. We issued \$281.0 million and \$135.9 million of such debt in the three-month periods ended March 31, 2006 and 2005 respectively. Cash used in financing activities includes the repayment of securitization trust debt of \$105.0 million and \$59.6 million for the three-month periods ended March 31, 2006 and 2005, respectively.

We purchase automobile contracts from dealers for a cash price approximating their principal amount, adjusted for an acquisition fee which may either increase or decrease the automobile contract purchase price. Those automobile contracts generate cash flow, however, over a period of years. As a result, we have been dependent on warehouse credit facilities to purchase automobile contracts, and on the availability of cash from outside sources in order to finance our continuing operations, as well as to fund the portion of automobile contract purchase prices not financed under revolving warehouse credit facilities. As of March 31, 2006, we had \$350 million in warehouse credit capacity,

in the form of a \$150 million facility and \$200 million facility. The \$200 million facility provides funding for automobile contracts purchased under the TFC Programs while both warehouse facilities provide funding for automobile contracts purchased under the CPS Programs. On June 29, 2005, we terminated a third facility in the amount of \$125 million, which we had utilized to fund automobile contracts under the CPS and TFC Programs.

The first of two warehouse facilities mentioned above is structured to allow us to fund a portion of the purchase price of automobile contracts by drawing against a floating rate variable funding note issued by our

consolidated subsidiary Page Three Funding, LLC. This facility was established on November 15, 2005, and expires on November 14, 2006, although it is renewable with the mutual agreement of the parties. Up to 80% of the principal balance of automobile contracts may be advanced to us under this facility, subject to collateral tests and certain other conditions and covenants. Notes under this facility accrue interest at a rate of one-month LIBOR plus 2.00% per annum. At March 31, 2006, \$171,000 was outstanding under this facility.

The second of two warehouse facilities is similarly structured to allow us to fund a portion of the purchase price of automobile contracts by drawing against a floating rate variable funding note issued by our consolidated subsidiary Page Funding LLC. This facility was entered into on June 30, 2004. On June 29, 2005 the facility was increased from \$100 million to \$125 million and further amended to provide for funding for automobile contracts purchased under the TFC programs, in addition to our CPS programs. The available credit under the facility was increased again to \$200 million on August 31, 2005. In February 2006, the terms of this facility were amended to allow advances to us of up to 80% of the principal balance of automobile contracts that we purchase under our CPS programs, and of up to 70% of the principal balance of automobile contracts that we purchase under our TFC programs, in all events subject to collateral tests and certain other conditions and covenants. Notes under this facility accrue interest at a rate of one-month LIBOR plus 2.00% per annum. The lender has annual termination options at its sole discretion on each June 30 through 2007, at which time the agreement expires. At March 31, 2006, \$74.9 million was outstanding under this facility.

The balance outstanding under these warehouse facilities generally will increase as we purchase additional automobile contracts, until we effect a securitization utilizing automobile contracts warehoused in the facilities, at which time the balance outstanding will decrease.

We securitized \$202.3 million of automobile contracts in one private placement transaction during the three months ended March 31, 2006, and \$674.4 million of automobile contracts in five private placement transactions during the year ended December 31, 2005, as compared to \$463.9 million in five private placements during the year ended December 31, 2004. All of these transactions were structured as secured financings and, therefore, resulted in no gain on sale. During the year ended December 31, 2003, we securitized \$416.9 million of automobile contracts in four private placement transactions. The first two such transactions of 2003 were structured as sales for financial accounting purposes, resulting in a gain on sale of \$6.4 million (net of a negative fair value adjustment of \$4.1 million related to the performance of previously securitized pools). The final two transactions of 2003 were structured as secured financings and, therefore, resulted in no gain on sale. In March 2004, one of our wholly-owned bankruptcy remote consolidated subsidiaries issued \$44.0 million of asset-backed notes secured by its retained interest in eight term securitization transactions. The notes had an interest rate of 10.0% per annum and a final maturity in October 2009 and were required to be repaid from the distributions on the underlying retained interests. In connection with the issuance of the notes, we incurred and capitalized issuance costs of \$1.3 million. We repaid the notes in full in August 2005. In November 2005, we completed a similar securitization whereby a wholly-owned bankruptcy remote consolidated subsidiary of ours issued \$45.8 million of asset-backed notes secured by its retained interest in 10 term securitization transactions. These notes, which bear interest at a blended interest rate of 8.36% per annum and have a final maturity in July 2011, are required to be repaid from the distributions on the underlying residual interests. In connection with the issuance of the notes, we incurred and capitalized issuance costs of \$915,000.

For the portfolio owned by non-consolidated subsidiaries, cash used to increase credit enhancement amounts to required levels for the years ended December 31, 2005, 2004 and 2003 was zero, \$2.9 million, \$20.9 million, respectively. Cash released from trusts and their related spread accounts to us related to the portfolio owned by consolidated subsidiaries for the years ended December 31, 2005, 2004 and 2003 was \$23.1 million, \$21.4 million and \$25.9 million, respectively. Changes in the amount of credit enhancement required for term securitization transactions and releases from trusts and their related spread accounts are affected by the relative size, seasoning and performance of the various pools of automobile contracts securitized that make up our managed portfolio to which the respective spread accounts are related. During the years ended December 31, 2005 and December 31, 2004, we made no initial deposits to spread accounts and funded no initial overcollateralization related to our term securitization transactions

owned by non-consolidated subsidiaries, compared to \$18.7 million in 2003.

For the portfolio owned by consolidated subsidiaries, cash used to establish or increase spread accounts for the three-month periods ended March 31, 2006 and 2005 was \$6.1 million and \$3.2 million, respectively. Cash released from trusts and their related spread accounts to our for the three-month periods ended March 31, 2006 and 2005, was \$3.9 million and \$8.0 million, respectively

The acquisition of automobile contracts for subsequent sale in securitization transactions, and the need to fund spread accounts and initial overcollateralization, if any, and increase credit enhancement levels when those transactions take place, results in a continuing need for capital. The amount of capital required is most heavily dependent on the rate of our automobile contract purchases, the required level of initial credit enhancement in securitizations, and the extent to which the previously established trusts and their related spread accounts either release cash to us or capture cash from collections on securitized automobile contracts. We may be limited in our ability to purchase automobile contracts due to limits on our capital. As of December 31, 2005, we had unrestricted cash on hand of \$17.8 million and available capacity from our warehouse credit facilities of \$314.6 million. As of March 31, 2006, we had unrestricted cash on hand of \$25.5 million and available capacity from our warehouse credit facilities of \$274.9 million. Warehouse capacity is subject to the availability of suitable automobile contracts to serve as collateral and of sufficient cash to fund the portion of such automobile contracts purchase price not advanced under the warehouse facilities. Our plans to manage the need for liquidity include the completion of additional securitizations that would provide additional credit availability from the warehouse credit facilities, and matching our levels of automobile contract purchases to our availability of cash. There can be no assurance that we will be able to complete securitizations on favorable economic terms or that we will be able to complete securitizations at all. If we are unable to complete such securitizations, we may be unable to purchase automobile contracts and interest income and other portfolio related income would decrease.

Our primary means of ensuring that our cash demands do not exceed our cash resources is to match our levels of automobile contract purchases to our availability of cash. Our ability to adjust the quantity of automobile contracts that we purchase and securitize will be subject to general competitive conditions and the continued availability of warehouse credit facilities. There can be no assurance that the desired level of automobile contract purchases can be maintained or increased. While the specific terms and mechanics of each spread account vary among transactions, our securitization agreements generally provide that we will receive excess cash flows only if the amount of credit enhancement has reached specified levels and/or the delinquency, defaults or net losses related to the automobile contracts in the pool are below certain predetermined levels. In the event delinquencies, defaults or net losses on the automobile contracts exceed such levels, the terms of the securitization: (i) may require increased credit enhancement to be accumulated for the particular pool; (ii) may restrict the distribution to us of excess cash flows associated with other pools; or (iii) in certain circumstances, may permit the insurers to require the transfer of servicing on some or all of the automobile contracts to another servicer. There can be no assurance that collections from the related trusts will continue to generate sufficient cash.

Certain of our securitization transactions and the warehouse credit facilities contain various financial covenants requiring certain minimum financial ratios and results. Such covenants include maintaining minimum levels of liquidity and net worth and not exceeding maximum leverage levels and maximum financial losses. In addition, certain securitization and non-securitization related debt contain cross-default provisions that would allow certain creditors to declare a default if a default occurred under a different facility.

The agreements under which we receive periodic fees for servicing automobile contracts in securitizations are terminable by the respective note insurers upon defined events of default, and, in some cases, at the will of the note insurer. Were a note insurer in the future to exercise its option to terminate such agreements, such a termination could have a material adverse effect on our liquidity and results of operations, depending on the number and value of the terminated agreements. Our note insurers continue to extend our term as servicer on a monthly and/or quarterly basis, pursuant to the servicing agreements.

### ***Contractual Obligations***

The following table summarizes our material contractual obligations as of December 31, 2005 (dollars in thousands):

#### **Payment due by period (1)**

	<b>Total</b>	<b>Less Than 1 Year</b>	<b>1 to 3 Years</b>	<b>3 to 5 Years</b>	<b>More Than 5 Years</b>
Long term debt (2)(3)	\$ 58,866	\$ 55,854	\$ 2,642	\$ 279	\$ 91
Operating leases (1)	11,085	4,353	6,188	545	

Securitization trust debt, in the aggregate amount of \$924.0 million as of December 31, 2005, is omitted from this table because it becomes due as and when the related receivables balance is reduced. Expected payments, which will depend on the performance of such receivables, as to which there can be no assurance, are \$328.7 million in 2006, \$223.7 million in 2007, \$160.5 million in 2008, \$114.6 million in 2009,

\$75.1 million in 2010, and \$21.4 million in 2011. Residual interest financing, of \$43.7 million as of December 31, 2005, is also omitted from this table because it becomes due as and when the related residual interest and Spread account balances are reduced. Expected payments, which will depend on the performance of the related receivables, as to which there can be no assurance, are \$18.0 million in 2006, \$14.4 million in 2007, \$7.6 million in 2008 and \$3.7 million in 2009.

(2)

On May 26, 2006, the due date of \$25.0 million of long-term debt held by Levine Leichtman, which was due in less than one year (on May 27, 2006 and June 24, 2006, respectively) was amended to May 31, 2007. The remaining \$15.0 million of long-term debt held by Levine Leichtman is due in December 2006. See Certain Transactions. An additional \$14.0 million of subordinated debt, not held by this selling shareholder, was paid when due in January 2006.

(3)

Long term debt includes senior secured debt, subordinated debt, subordinated renewable notes and notes payable.

### ***Warehouse Credit Facilities***

The terms on which credit has been available to us for purchase of automobile contracts have varied over the three years 2004-2006 and through March 31, 2006, as shown in the following recapitulation of our warehouse credit facilities:

*Facility in use from November 2000 to February 2004.* In November 2000, we (through our subsidiary CPS Funding LLC) entered into a floating rate variable note purchase facility under which up to \$75.8 million of notes could be outstanding at any time subject to collateral tests and other conditions. We used funds derived from this facility to purchase automobile contracts under the CPS Programs, which were pledged to secure the notes. The collateral tests and other conditions generally allowed us to borrow up to approximately 72.5% of the principal balance of the automobile contracts. Notes issued under this facility bore interest at one-month LIBOR plus 0.75% per annum. This facility expired on February 21, 2004.

*Facility in use from March 2002 to June 2005.* In March 2002, we (through our subsidiary CPS Warehouse Trust) entered into a second floating rate variable note purchase facility, under which up to \$125.0 million of notes could be outstanding at any time, subject to collateral tests and other conditions. We used funds derived from this facility to purchase automobile contracts under the CPS Programs and the TFC Programs, which were pledged to secure the notes. The collateral tests and other conditions generally allowed us to borrow up to approximately 73% of the principal balance of the automobile contracts purchased under the CPS Programs. Notes issued under this facility bore interest at commercial paper plus 1.18% per annum. During November 2004, this facility was amended to allow us to borrow up to approximately 70% of the principal balance of automobile contracts purchased under the TFC Programs. This facility was due to expire on April 11, 2006, but we elected to terminate it on June 29, 2005.

*Facility in use from May 2003 to June 2004.* In connection with the TFC merger in May 2003, we (through our subsidiary TFC Warehouse I LLC) entered into a third floating rate variable note purchase facility, under which up to \$25.0 million of notes could be outstanding at any time, subject to collateral tests and other conditions. We used funds derived from this facility to purchase automobile contracts under the TFC Programs, which were pledged to secure the notes. The collateral tests and other conditions generally allowed us to borrow up to approximately 71% of the principal balance of the automobile contracts. Notes issued under this facility bore interest at LIBOR plus 1.75% per annum. This facility expired on June 24, 2004.



*Facility in use from June 2004 to present.* In June 2004, we (through our subsidiary Page Funding LLC) entered into a floating rate variable note purchase facility. Up to \$200.0 million of notes may be outstanding under this facility at any time subject to certain collateral tests and other conditions. We use funds derived from this facility to purchase automobile contracts under the CPS Programs and TFC Programs, which are pledged to secure the notes. The collateral tests and other conditions generally allow us to borrow up to approximately 80% of the principal balance of automobile contracts that we purchase under our CPS programs, and of up to 70% of the principal balance of automobile contracts that we purchase under our TFC programs. Notes issued under this facility bear interest at one-month LIBOR plus 2.00% per annum. The balance of notes outstanding related to this facility at December 31, 2005 was \$836,000 and at March 31, 2006 was \$74.9 million.

*Facility in use from November 2005 to present.* In November 2005, we (through our subsidiary Page Three Funding LLC) entered into a floating rate variable note purchase facility. Up to \$150 million of notes may be outstanding under this facility at any time subject to certain collateral tests and other conditions. We use funds derived from this facility to purchase automobile contracts under the CPS Programs, which are pledged to secure the notes. The collateral tests and other conditions generally allow us to borrow up to approximately 80.0% of the principal balance of the automobile contracts. Notes issued under this facility bear interest at one-month LIBOR plus 2.00% per annum. The balance of notes outstanding related to this facility at December 31, 2005 was \$34.5 million and at March 31, 2006 was \$171,000.

***Capital Resources***

As noted above, approximately \$15.0 million of long-term debt matures in December 2006, and an additional \$25.0 million of long-term debt matures in May 2007. We plan to repay our long-term debt from a combination of the following: (i) additional proceeds from the offering of subordinated renewable notes; (ii) a possible transaction similar to the financings that we undertook in March 2004 and November 2005, where we issued notes secured by our residual interests in securitizations; and (iii) possible senior secured financing similar to our existing outstanding senior secured financing. There can be no assurance that we will be able to complete these transactions. Securitization trust debt is repaid from collections on the related receivables, and becomes due in accordance with its terms as the principal amount of the related receivables is reduced. Although the securitization trust debt also has alternative maximum maturity dates, those dates are significantly later than the dates at which repayment of the related receivables is anticipated, and at no time in our history have any of our sponsored asset-backed securities reached those alternative maximum maturities.

The acquisition of automobile contracts for subsequent transfer in securitization transactions, and the need to fund spread accounts and initial overcollateralization, if any, when those transactions take place, results in a continuing need for capital. The amount of capital required is most heavily dependent on the rate of our automobile contract purchases, the required level of initial credit enhancement in securitizations, and the extent to which the trusts and related spread accounts either release cash to us or capture cash from collections on securitized automobile contracts. We plan to adjust our levels of automobile contract purchases so as to match anticipated releases of cash from the trusts and related spread accounts with our capital requirements.

**Capitalization**

Over the period from January 1, 2003 through March 31, 2006 we have managed our capitalization by issuing and restructuring debt as summarized in the following table:

	<b>Three Months</b>			
	<b>Ended March 31, 2006</b>	<b>2005</b>	<b>Year Ended December 31,</b>	
	<b>(unaudited)</b>		<b>2004</b>	<b>2003</b>
			<b>(Dollars in thousands)</b>	
<b>Residual interest financing:</b>				
Beginning balance	\$ 43,745	\$ 22,204	\$	\$
Issuances		45,800	44,000	
Payments	(6,017 )	(24,259	(21,796	
Ending balance	\$ 37,728	\$ 43,745	\$ 22,204	\$
<b>Securitization trust debt:</b>				
Beginning balance	\$ 924,026	\$ 542,815	\$ 245,118	\$ 71,630
Assumption in connection with TFC Merger				115,597
Issuances	280,977	662,350	474,720	154,735
Payments	(104,397 )	(281,139 )	(177,023 )	(96,484 )
Ending balance	\$ 1,100,606	\$ 924,026	\$ 542,815	\$ 245,118
<b>Senior secured debt:</b>				
Beginning balance	\$ 40,000	\$ 59,829	\$ 49,965	\$ 50,072
Issuances			25,000	25,000
Payments		(19,829 )	(15,136 )	(25,107 )
Ending balance	\$ 40,000	\$ 40,000	\$ 59,829	\$ 49,965
<b>Subordinated debt:</b>				
Beginning balance	\$ 14,000	\$ 15,000	\$ 35,000	\$ 36,000
Payments	(14,000 )	(1,000 )	(20,000 )	(1,000 )
Ending balance	\$	\$ 14,000	\$ 15,000	\$ 35,000
<b>Subordinated renewable notes:</b>				
Beginning balance	\$4,655	\$	\$	\$
Issuances	1,701	4,685		
Payments	(42 )	(30 )		
Ending balance	\$6,314	\$ 4,655	\$	\$
<b>Related party debt:</b>				

Beginning balance	\$	\$	17,500	\$	17,500
Non-cash conversion			(1,000 )		
Payments			(16,500 )		
Ending balance	\$	\$		\$	17,500

*Residual Interest Financing.* In March 2004, one of our wholly-owned bankruptcy remote consolidated subsidiaries issued \$44.0 million of asset-backed notes secured by our retained interests in eight term securitization transactions. We repaid the notes in full in August 2005. In November 2005, we completed a similar securitization whereby a wholly-owned bankruptcy remote consolidated subsidiary of ours issued \$45.8 million of asset-backed notes secured by our retained interests in 10 term securitization transactions. These notes have a final maturity in July 2011, and are required to be repaid from the distributions on the underlying retained interests.

*Securitization Trust Debt.* Since the third quarter of 2003, we have for financial accounting purposes, treated securitizations of automobile contracts as secured financings, and the asset-backed securities issued in such

securitizations remain on our balance sheet as securitization trust debt. In addition, in connection with the MFN merger in March 2002 and the TFC merger in May 2003 we assumed \$156.9 million and \$115.6 million, respectively, of securitization trust debt related to finance receivables that had been previously securitized in securitization transactions accounted for as secured financings.

*Senior Secured Debt.* Since 1998, we have entered into a series of financing transactions with Levine Leichtman to provide us with funding in the form of issuances of our debt securities to it. For additional details on our existing senior secured notes, see Certain Transactions.

*Subordinated Debt.* In April 1997, we issued \$20.0 million in subordinated participating equity notes due April 2004, which we retired in the second quarter of 2004. In 1995, we issued \$20.0 million of Rising Interest Subordinated Redeemable Securities, or RISRS, due 2006. The RISRS included a sinking fund in their terms, and we repaid in the first quarter of 2006 the \$14.0 million that remained outstanding. In May 2003, in connection with the acquisition of TFC, we assumed \$6.3 million in principal amount of subordinated debt that TFC had outstanding. We amortized this debt monthly and repaid it in full in June 2005.

*Subordinated Renewable Notes Debt.* In June 2005, we began issuing registered subordinated renewable notes. Upon maturity, the notes will be automatically renewed for the same term as the maturing notes, unless we elect not to have the notes renewed or unless the investor notifies us within 15 days after the maturity date for his notes that he wants his notes repaid. Renewed notes will bear interest at the rate we are offering at that time to other investors with similar aggregate note portfolios. Based on the terms of the individual notes, interest payments may be required monthly, quarterly, annually or upon maturity.

*Related Party Debt.* In June 1997 we borrowed \$15.0 million from one of the selling shareholders, Stanwich Financial Services Corp., or Stanwich, which was an affiliated corporation at that time. This debt was due in 2004 and we repaid it in the second quarter of 2004. During 1999 we borrowed another \$1.5 million from Stanwich, which we also repaid in the second quarter of 2004. During 1998 we borrowed \$1.0 million from one of our directors. In the second quarter of 2004 our indebtedness to that director was converted, in accordance with its terms, into common stock at the rate of \$3.00 per share.

We must comply with certain affirmative and negative covenants related to debt facilities, which require, among other things, that we maintain certain financial ratios related to liquidity, net worth, capitalization, investments, acquisitions, restricted payments and certain dividend restrictions. As a result of waivers and amendments to covenants related to securitization and non-securitization related debt throughout 2004 and 2005, we were in compliance with all such covenants as of March 31, 2006. In addition, certain securitization and non-securitization related debt contain cross-default provisions that would allow certain creditors to declare default if a default occurred under a different facility.

## OUR COMPANY

### Overview

We are a specialty finance company engaged in purchasing and servicing retail automobile contracts originated primarily by franchised automobile dealers and to a lesser extent by select independent dealers in the United States in the sale of new and used automobiles, light trucks and passenger vans. Through our automobile contract purchases, we provide indirect financing to the customers of dealers, who have limited credit histories, low incomes or past credit problems, who we refer to as sub-prime customers. We serve as an alternative source of financing for dealers, facilitating sales to customers who otherwise might not be able to obtain financing from traditional sources, such as commercial banks, credit unions and the captive finance companies affiliated with major automobile manufacturers. We do not lend money directly to consumers but, rather, purchase automobile contracts from dealers under several different financing programs. We are headquartered in Irvine, California, where all credit and underwriting functions are centralized. We service our automobile contracts from our California headquarters and from three strategically located servicing branches in Virginia, Florida and Illinois.

We direct our marketing efforts to dealers, rather than to consumers. We establish relationships with dealers through marketing representatives who contact a prospective dealer to explain our automobile contract purchase programs, and thereafter provide dealer training and support services. The marketing representatives are obligated to represent our financing program exclusively. Our marketing representatives present the dealer with a marketing package, which includes our promotional material containing the terms offered by us for the purchase of automobile contracts, a copy of our standard-form dealer agreement, and required documentation relating to automobile contracts. As of March 31, 2006, we had 84 marketing representatives and we were a party to dealer agreements with over 7,300 dealers in 47 states. Approximately 92% of these dealers are franchised new car dealers that sell both new and used cars and the remainder are independent used car dealers. For the year ended December 31, 2005, approximately 81% of the automobile contracts purchased under our programs consisted of financing for used cars and 19% consisted of financing for new cars, as compared to 85% financing for used cars and 15% for new cars in the year ended December 31, 2004.

We purchase automobile contracts with the intention of financing them on a long-term basis through securitizations. Securitizations are transactions in which we sell a specified pool of contracts to a special purpose entity of ours, which in turn issues asset-backed securities to fund the purchase of the pool of contracts from us. Depending on the structure of the securitization, the transaction may, for financial accounting purposes, be treated as a sale of the contracts or as a secured financing. From inception through the third quarter of 2003, we generated revenue primarily from the gains recognized on the sale or securitization of automobile contracts, servicing fees earned on automobile contracts sold, interest earned on residual interests and interest on finance receivables. However, since the third quarter of 2003, we have structured our securitizations to be treated as secured financings rather than as sales of automobile contracts for financial accounting purposes. By accounting for these securitizations as secured financings, the contracts and asset-backed notes issued remain on our balance sheet with the interest income of the contracts in the trust and the related financing costs reflected over the life of the underlying pool of contracts.

We were incorporated and began our operations in October 1991. From inception through March 31, 2006, we have purchased a total of approximately \$6.3 billion of automobile contracts from dealers. In addition, we obtained a total of approximately \$605.0 million of automobile contracts in our 2002, 2003 and 2004 acquisitions, as described below. Our total managed portfolio, net of unearned interest on pre-computed automobile contracts, grew to approximately \$1,240.0 million at March 31, 2006 from \$1,122.0 million at December 31, 2005, \$906.9 million as of December 31, 2004 and \$743.5 million as of December 31, 2003.

### *Historical Acquisitions*

In March 2002, we acquired MFN Financial Corporation and its subsidiaries, or MFN, in a merger, which we refer to as the MFN merger. In May 2003, we acquired TFC Enterprises, Inc. and its subsidiaries, or TFC, in a second merger, which we refer to as the TFC merger. We acquired \$381.8 million of automobile contracts in the MFN merger, and \$152.1 million in the TFC merger. MFN and TFC were engaged in businesses similar to that of ours. MFN ceased acquiring automobile contracts in March 2002, while TFC continues to acquire automobile contracts under its TFC programs. Automobile contracts purchased by TFC during the year ended December 31, 2005 accounted for less than 5% of our total purchases during the year. In April 2004, we acquired \$74.9 million in

automobile contracts from SeaWest Financial Corporation and its subsidiaries. In addition, we were named servicer of approximately \$111.8 million of automobile contracts that SeaWest had previously securitized.

### ***Sub-Prime Auto Finance Industry***

Automobile financing is the second largest consumer finance market in the United States. The automobile finance industry can be divided into two principal segments: a prime credit market and a sub-prime credit market. Traditional automobile finance companies, such as commercial banks, savings institutions, credit unions and captive finance companies of automobile manufacturers, generally lend to the most creditworthy, or so-called prime, borrowers. The non-prime automobile credit market, in which we operate, provides financing to borrowers who generally cannot obtain financing from traditional lenders.

Historically, traditional lenders have not serviced the sub-prime market or have done so only through programs that were not consistently available. Independent companies specializing in sub-prime automobile financing and subsidiaries of larger financial services companies currently compete in this segment of the automobile finance market, which we believe remains highly fragmented, with no single company having a significant share of the market.

### **Our Operations**

Our automobile financing programs are designed to serve sub-prime customers who generally would not qualify for automobile financing from traditional sources, such as commercial banks, credit unions and the captive finance companies affiliated with major automobile manufacturers, because they have limited credit histories, low incomes or past credit problems. Because we serve customers who are unable to meet the credit standards imposed by most traditional automobile financing sources, we generally receive interest rates higher than those charged by traditional automobile financing sources. We also sustain a higher level of credit losses than traditional automobile financing sources since we provide financing in a relatively high risk market.

### **Originations**

When a retail automobile buyer elects to obtain financing from a dealer, the dealer takes a credit application to submit to its financing sources. Typically, a dealer will submit the buyer's application to more than one financing source for review. We believe the dealer's decision to choose a financing source is based primarily on: (i) the monthly payment; (ii) the purchase price offered for the contract; (iii) timeliness, consistency and predictability of response; (iv) funding turnaround time; and (v) any conditions to purchase. Dealers can send credit applications to us via the Internet or fax. For the three months ended March 31, 2006, we received approximately 80% of all applications through DealerTrack (the industry leading dealership application aggregator), 10% via our website and 10% via fax. Our automated application decisioning system gave an almost instantaneous response to about 90% of those applications.

Upon receipt of information from a dealer, our proprietary automated decisioning system orders a credit report to document the buyer's credit history. If, upon review by the automated decisioning systems, or in some cases, one of our credit analysts, it is determined that the automobile contract meets our underwriting criteria, or would meet such criteria with modification, we request and review further information and supporting documentation and, ultimately, decide whether to approve the automobile contract for purchase. When presented with an application, we attempt to notify the dealer within one hour as to whether we would purchase the related automobile contract.

Most of the dealers under a dealer agreement with us regularly submit automobile contracts for purchase, although they are under no obligation to submit any automobile contracts to us, nor are we obligated to purchase any automobile contracts from them. During the year ended December 31, 2005, and the three month period ended March 31, 2006, no dealer accounted for more than 1% of the total number of automobile contracts we purchased. Automobile contracts purchased by TFC after the TFC merger under the TFC programs are purchased with a dealer



marketing strategy that is similar to that of ours as described above except that the marketing efforts are directed at independent used car dealers and the target obligors are enlisted personnel of the U.S. Armed Forces. The following table sets forth the geographical sources of the automobile contracts purchased by us (based on the addresses of the customers as stated on our records) during the three months ended March 31, 2006 and the years ended December 31, 2005 and 2004.

**Contracts Purchased (1) During the**

	<b>Three Months Ended</b>		<b>Year Ended</b>			
	<b>March 31, 2006</b>		<b>December 31, 2005</b>		<b>December 31, 2004</b>	
	<b>Number</b>	<b>Percent</b>	<b>Number</b>	<b>Percent</b>	<b>Number</b>	<b>Percent</b>
Texas	1,638	10.0 %	4,734	10.7 %	3,422	12.1 %
California	1,614	9.8	3,981	9.0	2,431	8.6
Ohio	1,299	7.9	3,311	7.5	1,437	5.1
Florida	1,109	6.8	3,151	7.1	1,731	6.1
Pennsylvania	883	5.4	2,732	6.2	1,676	5.9
Illinois	811	4.9	2,188	4.9	1,312	4.6
Louisiana	779	4.8	2,268	5.1	1,949	6.9
Michigan	733	4.5	1,883	4.2	1,121	4.0
Maryland	685	4.2	1,933	4.4	1,373	4.8
Kentucky	637	3.9	1,851	4.2	1,118	3.9
North Carolina	631	3.8	2,003	4.5	1,390	4.9
New York	611	3.7	1,617	3.6	1,102	3.9
Virginia	460	2.8	1,379	3.1	1,043	3.7
Georgia	353	2.2	1,277	2.9	1,263	4.5
Other States	4,151	24.5	10,068	22.7	6,008	21.2
<b>Total</b>	<b>16,394</b>	<b>100.0 %</b>	<b>44,376</b>	<b>100.0 %</b>	<b>28,376</b>	<b>100.0 %</b>

(1)

Automobile contracts purchased by TFC after the TFC merger are not included because such purchases accounted for less than 10% of the total purchases during the year.

We purchase automobile contracts under our programs from dealers at a price generally equal to the total amount financed under the automobile contracts, adjusted for an acquisition fee, which may either increase or decrease the automobile contract purchase price paid by us. The amount of the acquisition fee, and whether it results in an increase or decrease to the automobile contract purchase price, is based on the perceived credit risk and, in some cases, the interest rate on the automobile contract. For the years ended December 31, 2005, 2004 and 2003, the average acquisition fee charged per automobile contract purchased under our programs was \$150, \$226 and \$372, respectively, or 1.0%, 1.6% and 2.7%, respectively, of the amount financed.

We offer seven different financing programs to our dealership customers, and price each program according to the relative credit risk. We offer programs covering a wide band of the credit spectrum. Our upper credit tier products, which are our Preferred, Super Alpha, Alpha Plus and Alpha programs accounted for approximately 82% of our new contract originations in 2005 and 80% for the three months ended March 31, 2006, in each case measured by aggregate amount financed.

The following table identifies the credit program, sorted from highest to lowest credit quality, under which we purchased automobile contracts during the three months ended March 31, 2006 and the years ended December 31, 2005 and 2004.

**Contracts Purchased (1) During the**

(dollars in thousands)	<b>Three Months Ended</b>			<b>Year Ended</b>			
	<b>March 31, 2006</b>			<b>December 31, 2005</b>		<b>December 31, 2004</b>	
	<b>Amount</b>	<b>Percent</b>		<b>Amount</b>	<b>Percent</b>	<b>Amount</b>	<b>Percent</b>
Preferred	\$ 4,567	1.9 %		\$ 13,735	2.1 %	\$ 6,273	1.5 %
Super Alpha	30,027	12.2		78,030	11.8	34,134	8.3
Alpha Plus	48,707	19.7		135,926	20.6	70,786	17.3
Alpha	113,423	46.0		314,444	47.6	233,521	57.1
Standard	19,734	8.0		67,293	10.2	36,561	8.9
Mercury/Delta	17,265	7.0		20,346	3.1	9,988	2.4
First Time Buyer	12,947	5.2		30,329	4.6	17,655	4.3
	\$ 246,670	100.0 %		\$ 660,103	100.0 %	\$ 408,918	100.0 %

(1)

Automobile contracts purchased by TFC after the TFC merger are not included because such purchases accounted for less than 10% of the total purchases during the year.

(2)

Percentages may not total to 100.0% due to rounding.

We attempt to control misrepresentation regarding the customer's credit worthiness by carefully screening the automobile contracts we purchase, by establishing and maintaining professional business relationships with dealers, and by including certain representations and warranties by the dealer in the dealer agreement. Pursuant to the dealer agreement, we may require the dealer to repurchase any automobile contract in the event that the dealer breaches our representations or warranties. There can be no assurance, however, that any dealer will have the willingness or the financial resources to satisfy our repurchase obligations to us.

## **Underwriting**

To be eligible for purchase by us, an automobile contract must have been originated by a dealer that has entered into a dealer agreement to sell automobile contracts to us. The automobile contract must be secured by a first priority lien on a new or used automobile, light truck or passenger van and must meet our underwriting criteria. In addition, each automobile contract requires the customer to maintain physical damage insurance covering the financed vehicle and naming us as a loss payee. We may, nonetheless, suffer a loss upon theft or physical damage of any financed vehicle if the customer fails to maintain insurance as required by the automobile contract and is unable to pay for repairs to or replacement of the vehicle or is otherwise unable to fulfill his or her obligations under the automobile contract.

We believe that our underwriting criteria enable us to evaluate effectively the creditworthiness of sub-prime customers and the adequacy of the financed vehicle as security for an automobile contract. The underwriting criteria include standards for price, term, amount of down payment, installment payment and interest rate; mileage, age and type of vehicle; principal amount of the automobile contract in relation to the value of the vehicle; customer income level, employment and residence stability, credit history and debt service ability, as well as other factors. Specifically, our underwriting guidelines generally limit the maximum principal amount of a purchased automobile contract to 115% of wholesale book value in the case of used vehicles or to 115% of the manufacturer's invoice in the case of new vehicles, plus, in each case, sales tax, licensing and, when the customer purchases such additional items, a service contract or a credit life or disability policy. We generally do not finance vehicles that are more than eight model years old or have in excess of 85,000 miles. Under most of our programs, the maximum term of a purchased contract is 72 months; a shorter maximum term may be applicable based on the mileage and age of the vehicle. Automobile contracts with the maximum term of 72 months may be purchased if the customer is among the more creditworthy of our obligors and the vehicle is generally not more than two model years old and has less than 35,000 miles. Automobile contract purchase criteria are subject to change from time to time as circumstances may warrant. Upon receiving the vehicle and customer information with the customer's application, our underwriters verify the customer's employment, residency, and credit information by contacting various parties noted on the customer's application, credit information bureaus and other sources. In addition, prior to purchasing an automobile contract, we contact each customer by telephone to confirm that the customer understands and agrees to the terms of the related automobile contract. During this welcome call, we also ask the customer a series of open ended questions about his application and the contract to uncover any potential misrepresentations.

*Credit Scoring.* We use a proprietary scoring model to assign each automobile contract a credit score at the time the application is received from the dealer and the customer's credit information is retrieved from the credit reporting agencies. The credit score is based on a variety of parameters, such as the customer's employment and residence stability, the customer's income, the monthly payment amount, the loan-to-value ratio and the age and mileage of the vehicle. We have developed the credit score utilizing statistical risk management techniques and historical performance data from our managed portfolio. We believe this improves our allocation of credit evaluation resources, and more effectively manages the risk inherent in the sub-prime market.

*Characteristics of Contracts.* All of the automobile contracts purchased by us are fully amortizing and provide for level payments over the term of the automobile contract. All automobile contracts may be prepaid at any time without penalty. The average original principal amount financed, under the CPS programs and in the year ended December 31, 2005, was \$14,875, with an average original term of 62 months and an average down payment amount of 13.4%. Based on information contained in customer applications for this 12-month period, the retail purchase price of the

related automobiles averaged \$15,278 (which excludes tax, license fees and any additional costs such as a maintenance contract), the average age of the vehicle at the time the automobile contract was purchased was 3 years, and our customers averaged approximately 38 years of age, with approximately \$39,596 in average annual household income and an average of 5.0 years history with his or her current employer.

*Dealer Compliance.* The dealer agreement and related assignment contain representations and warranties by the dealer that an application for state registration of each financed vehicle, naming us as secured party with respect to the vehicle, was effected at the time of sale of the related automobile contract to us, and that all necessary steps have been taken to obtain a perfected first priority security interest in each financed vehicle in favor of us under the laws of the state in which the financed vehicle is registered.

## **Servicing and Collection**

We currently service all automobile contracts that we own as well as those automobile contracts included in portfolios that we have sold to off balance sheet securitization trusts. We organize our servicing activities based on the tasks performed by our personnel. Our servicing activities consist of mailing monthly billing statements; collecting, accounting for and posting of all payments received; responding to customer inquiries; taking all necessary action to maintain the security interest granted in the financed vehicle or other collateral; investigating delinquencies; communicating with the customer to obtain timely payments; repossessing and liquidating the collateral when necessary; collecting deficiency balances; and generally monitoring each automobile contract and the related collateral. We are typically entitled to receive a base monthly servicing fee between 2.5% and 3.5% per annum computed as a percentage of the declining outstanding principal balance of the non-charged-off automobile contracts in the securitization pools. The servicing fee is included in interest income for on balance sheet financings.

*Collection Procedures.* We believe that our ability to monitor performance and collect payments owed from sub-prime customers is primarily a function of our collection approach and support systems. We believe that if payment problems are identified early and our collection staff works closely with customers to address these problems, it is possible to correct many of problems before they deteriorate further. To this end, we utilize pro-active collection procedures, which include making early and frequent contact with delinquent customers; educating customers as to the importance of maintaining good credit; and employing a consultative and customer service approach to assist the customer in meeting his or her obligations, which includes attempting to identify the underlying causes of delinquency and cure them whenever possible. In support of our collection activities, we maintain a computerized collection system specifically designed to service automobile contracts with sub-prime customers and similar consumer obligations.

With the aid of our automatic dialer, as well as manual efforts made by collection staff, we typically attempt to make telephonic contact with delinquent customers on the sixth day after their monthly payment due date. Using coded instructions from a collection supervisor, the automatic dialer will attempt to contact customers based on their physical location, state of delinquency, size of balance or other parameters. If the automatic dialer obtains a no-answer or a busy signal, it records the attempt on the customer's record and moves on to the next call. If a live voice answers the automatic dialer's call, the call is transferred to a waiting collector as the customer's pertinent information is simultaneously displayed on the collector's workstation. The collector then inquires of the customer the reason for the delinquency and when we can expect to receive the payment. The collector will attempt to get the customer to make a promise for the delinquent payment for a time generally not to exceed one week from the date of the call. If the customer makes such a promise, the account is routed to a promise queue and is not contacted until the outcome of the promise is known. If the payment is made by the promise date and the account is no longer delinquent, the account is routed out of the collection system. If the payment is not made, or if the payment is made, but the account remains delinquent, the account is returned to the queue for subsequent contacts.

If a customer fails to make or keep promises for payments, or if the customer is uncooperative or attempts to evade contact or hide the vehicle, a supervisor will review the collection activity relating to the account to determine if repossession of the vehicle is warranted. Generally, such a decision will occur between the 45th and 90th day past the customer's payment due date, but could occur sooner or later, depending on the specific circumstances. At the time the vehicle is repossessed we will stop accruing interest in this automobile contract, and reclassify the remaining automobile contract balance to other assets. In addition we will apply a specific reserve to this automobile contract so that the net balance represents the estimated fair value less costs to sell.

If we elect to repossess the vehicle, we assign the task to an independent local repossession service. Such services are licensed and/or bonded as required by law. When the vehicle is recovered, the reposessor delivers it to a wholesale automobile auction, where it is kept until sold. Financed vehicles that have been repossessed are generally resold by us through unaffiliated automobile auctions, which are attended principally by car dealers. Net liquidation proceeds are applied to the customer's outstanding obligation under the automobile contract. Such proceeds usually are insufficient to pay the customer's obligation in full, resulting in a deficiency. In many cases we

will continue to contact our customers to recover all or a portion of this deficiency for up to several years after charge-off.

Once a automobile contract becomes greater than 90 days delinquent, we do not recognize additional interest income until the borrower under the automobile contract makes sufficient payments to be less than 90 days delinquent. Any payments received by a borrower that is greater than 90 days delinquent is first applied to accrued interest and then to principal reduction.

We generally charge off the balance of any contract by the earlier of the end of the month in which the automobile contract becomes five scheduled installments past due or, in the case of repossessions, the month that the proceeds from the liquidation of the financed vehicle are received by us or if the vehicle has been in repossession inventory for more than 90 days. In the case of repossession, the amount of the charge-off is the difference between the outstanding principal balance of the defaulted automobile contract and the net repossession sale proceeds.

### Credit Experience

Our financial results are dependent on the performance of the automobile contracts in which we retain an ownership interest. The tables below document the delinquency, repossession and net credit loss experience of all automobile contracts that we are servicing (excluding contracts from the SeaWest third party portfolio) as of the respective dates shown. Credit experience for us, MFN (since the date of the MFN merger), TFC (since the date of the TFC merger) and SeaWest (since the date of the SeaWest asset acquisition) is shown on a combined basis in the table below.

#### Delinquency Experience (1) CPS, MFN, TFC and SeaWest Combined

	March 31, 2006		December 31, 2005		December 31, 2004		December 31, 2003	
	Number of Contracts	Amount	Number of Contracts	Amount	Number of Contracts	Amount	Number of Contracts	Amount
30 days	1,250	12,795	2,367	24,047	2,106	19,010	2,506	17,000
60 days	564	5,215	1,057	10,156	1,069	8,051	1,340	8,000
90 days	575	4,066	1,031	7,946	1,176	7,758	1,522	9,000
Delinquencies	2,389	22,075	4,455	42,149	4,351	34,819	5,368	36,000
Repossessions	1,090	11,782	1,335	13,531	1,408	14,090	1,234	12,000
Net credit loss	\$ 3,479	\$ 33,857	\$ 5,790	\$ 55,680	\$ 5,759	\$ 48,909	\$ 6,602	\$ 48,000
Delinquencies								



Amount in possession									
Frequencies									
Percentage of									
Financing ratio	23 %	18 %	47 %	38 %	52 %	40 %	63 %		
Frequencies									
Amount in possession									
Percentage of									
Financing ratio	34 %	27 %	61 %	50 %	69 %	56 %	78 %		
<b>Delinquency</b>									
Contracts delinquent for 30 days or more	\$ 9,745	\$ 94,375	10,602	\$ 95,412	9,661	\$ 86,138	10,004	\$ 76,000	
Contracts delinquent for 31 days or more	3,480	26,903	4,575	29,428	4,383	23,659	7,347	34,000	
Contracts with delinquency (1)	\$ 13,225	\$ 121,278	\$ 15,177	\$ 124,840	14,044	\$ 109,797	17,351	\$ 110,000	

All amounts and percentages are based on the amount remaining to be repaid on each automobile contract, including, for pre-computed automobile contracts, any unearned interest. The information in the table represents the gross principal amount of all automobile contracts we purchased, including automobile contracts we subsequently sold in securitization transactions that we continue to service. The table does not include automobile contracts that we service on behalf of SeaWest securitizations, but do not own.

(2)

We consider an automobile contract delinquent when an obligor fails to make at least 90% of a contractually due payment by the following due date, which date may have been extended within limits specified in the servicing agreements. The period of delinquency is based on the number of days payments are contractually past due. Automobile contracts less than 31 days delinquent are not included.

(3)

Amount in repossession represents the contract balance on financed vehicles that have been repossessed but not yet liquidated. This amount is not netted with the specific reserve to arrive at the estimated asset value less costs to sell.

(4)

The aging categories shown in the tables reflect the effect of extensions.

## Extensions

We may offer a customer an extension, under which the customer agrees with us to move past due payments to the end of the automobile contract term. In such cases the customer must sign an agreement for the extension, and may pay a fee representing partial payment of accrued interest. Our policies, and contractual arrangements for our warehouse and securitization transactions, limit the number of extensions that may be granted. In general, a customer may arrange for an extension no more than once every 12 months, not to exceed four extensions over the life of the contract.

If a customer is granted such an extension, the date next due is advanced. Subsequent delinquency aging classifications would be based on the future payment performance of the automobile contract.

Net Charge-Off Experience (1) (in thousands)	Three Months Ended		Year Ended	
	March 31, 2006	2005	December 31, 2004	2003
CPS, MFN, TFC and SeaWest combined average managed portfolio outstanding	\$1,176,879	\$966,295	\$796,436	\$674,523
Net charge-offs as a percentage of average managed portfolio (2)	4.8%	5.3%	7.8%	6.8%

(1) All amounts and percentages are based on the principal amount scheduled to be paid on each automobile contract, net of unearned income on pre-computed automobile contracts. The information in the table represents all automobile contracts serviced by us (excluding automobile contracts originated by SeaWest for which we are the servicer but have no equity interest).

(2)

Net charge-offs include the remaining principal balance, after the application of the net proceeds from the liquidation of the vehicle (excluding accrued and unpaid interest) and amounts collected subsequent to the date of charge-off.

## Securitization of Automobile Contracts

We purchase automobile contracts with the intention of financing them on a long-term basis through securitizations. All such securitizations have involved identification of specific automobile contracts, sale of those automobile contracts (and associated rights) to a special purpose subsidiary, and issuance of asset-backed securities to fund the transactions. Upon the securitization of a portfolio of automobile contracts, we retain the obligation to service the contracts, and receive a monthly fee for doing so. We have been a regular issuer of asset-backed securities since 1994, completing 40 securitizations totaling over \$4.3 billion through March 31, 2006. Depending on the structure of the securitization, the transaction may be treated as a sale of the automobile contracts, or as a secured financing for financial accounting purposes. Since the third quarter of 2003, we have structured our securitizations as secured financings rather than as sales of contracts.

When structured to be treated as a secured financing, the subsidiary is consolidated and, accordingly, the automobile contracts and the related securitization trust debt appear as assets and liabilities, respectively, on our consolidated balance sheet. We then recognize interest income on the contracts and interest expense on the securities issued in the securitization and record as expense a provision for probable credit losses on the contracts.

When structured to be treated as a sale, the subsidiary is not consolidated. Accordingly, the securitization removes the sold automobile contracts from our consolidated balance sheet, and the asset-backed securities (debt of the non-consolidated subsidiary) do not appear as debt on our consolidated balance sheet, but rather show as an asset, a retained residual interest in the sold automobile contracts. The residual interest represents the discounted value of what we expect will be the excess of future collections on the automobile contracts over principal and interest due on the asset-backed securities and fees and other expenses. This residual interest appears on our consolidated balance sheet as Residual interest in securitizations, and its value is dependent on estimates of the future performance of the sold automobile contracts.

Prior to a securitization transaction, we fund our automobile contract purchases primarily with proceeds from warehouse credit facilities. As of March 31, 2006, we had \$350 million in warehouse credit capacity, in the form of a \$200 million facility and a \$150 million facility. Both warehouse credit facilities provide funding for automobile contracts purchased under the CPS programs, while the first facility also provides funding for automobile contracts purchased under the TFC programs. Up to 80% of the principal balance of the automobile contracts may be advanced to us under these facilities, subject to collateral tests and certain other conditions and covenants. Long-

term financing for the automobile contract purchases is achieved through securitization transactions and the proceeds from such securitization transactions are used primarily to repay the warehouse credit facilities.

In a securitization and in our warehouse credit facilities, we are required to make certain representations and warranties, which are generally similar to the representations and warranties made by dealers in connection with our purchase of the automobile contracts. If we breach any of our representations or warranties, we will be obligated to repurchase the automobile contract at a price equal to the principal balance plus accrued and unpaid interest. We may then be entitled under the terms of our dealer agreement to require the selling dealer to repurchase the contract at a price equal to our purchase price, less any principal payments made by the customer. Subject to any recourse against dealers, we will bear the risk of loss on repossession and resale of vehicles under automobile contracts that we repurchase.

Whether a securitization is treated as a secured financing or as a sale for financial accounting purposes, the related special purpose subsidiary may be unable to release excess cash to us if the credit performance of the securitized automobile contracts falls short of pre-determined standards. Such releases represent a material portion of the cash that we use to fund our operations. An unexpected deterioration in the performance of securitized automobile contracts could therefore have a material adverse effect on both our liquidity and results of operations, regardless of whether such automobile contracts are treated as having been sold or as having been financed. For estimation of the magnitude of such risk, it may be appropriate to look to the size of our managed portfolio, which represents both financed and sold automobile contracts as to which such credit risk is retained. Our managed portfolio as of March 31, 2006 was approximately \$1.2 billion (this amount includes \$12.5 million related to the SeaWest third party portfolio on which we earn only servicing fees and have no credit risk).

## **Competition**

The automobile financing business is highly competitive. We compete with a number of national, regional and local finance companies with operations similar to ours. In addition, competitors or potential competitors include other types of financial services companies, such as commercial banks, savings and loan associations, leasing companies, credit unions providing retail loan financing and lease financing for new and used vehicles, and captive finance companies affiliated with major automobile manufacturers such as General Motors Acceptance Corporation, Ford Motor Credit Corporation, Chrysler Finance Corporation and Nissan Motors Acceptance Corporation. Many of our competitors and potential competitors possess substantially greater financial, marketing, technical, personnel and other resources than we do. Moreover, our future profitability will be directly related to the availability and cost of our capital in relation to the availability and cost of capital to our competitors. Our competitors and potential competitors include far larger, more established companies that have access to capital markets for unsecured commercial paper and investment grade-rated debt instruments and to other funding sources that may be unavailable to us. Many of these companies also have long-standing relationships with dealers and may provide other financing to dealers, including floor plan financing for the dealers purchase of automobiles from manufacturers, which we do not offer.

We believe that the principal competitive factors affecting a dealer's decision to offer automobile contracts for sale to a particular financing source are the purchase price offered for the automobile contracts, the reasonableness of the financing source's underwriting guidelines and documentation requests, the predictability and timeliness of purchases and the financial stability of the funding source. While we believe that we can obtain from dealers sufficient automobile contracts for purchase at attractive prices by consistently applying reasonable underwriting criteria and making timely purchases of qualifying automobile contracts, there can be no assurance that we will do so.

## **Regulation**

Several federal and state consumer protection laws, including the federal Truth-In-Lending Act, the federal Equal Credit Opportunity Act, the federal Fair Debt Collection Practices Act and the Federal Trade Commission Act, regulate the extension of credit in consumer credit transactions. These laws mandate certain disclosures with respect to

finance charges on automobile contracts and impose certain other restrictions on dealers. In many states, a license is required to engage in the business of purchasing automobile contracts from dealers. In addition, laws in a number of states impose limitations on the amount of finance charges that may be charged by dealers on credit sales. The so-called Lemon Laws enacted by various states provide certain rights to purchasers with respect to automobiles that fail to satisfy express warranties. The application of Lemon Laws or violation of such other federal and state

laws may give rise to a claim or defense of a customer against a dealer and its assignees, including us and purchasers of automobile contracts from us. The dealer agreement contains representations by the dealer that, as of the date of assignment of automobile contracts, no such claims or defenses have been asserted or threatened with respect to the automobile contracts and that all requirements of such federal and state laws have been complied with in all material respects. Although a dealer would be obligated to repurchase automobile contracts that involve a breach of such warranty, there can be no assurance that the dealer will have the financial resources to satisfy our repurchase obligations. Certain of these laws also regulate our servicing activities, including our methods of collection.

Although we believe that we are currently in material compliance with applicable statutes and regulations, there can be no assurance that we will be able to maintain such compliance. The past or future failure to comply with such statutes and regulations could have a material adverse effect upon us. Furthermore, the adoption of additional statutes and regulations, changes in the interpretation and enforcement of current statutes and regulations or the expansion of our business into jurisdictions that have adopted more stringent regulatory requirements than those in which we currently conduct business could have a material adverse effect upon us. In addition, due to the consumer-oriented nature of the industry in which we operate and the application of certain laws and regulations, industry participants are regularly named as defendants in litigation involving alleged violations of federal and state laws and regulations and consumer law torts, including fraud. Many of these actions involve alleged violations of consumer protection laws. A significant judgment against us or within the industry in connection with any such litigation could have a material adverse effect on our financial condition, results of operations or liquidity.

### **Employees**

As of May 31, 2006, we had 715 full-time and five part-time employees. The breakdown of the employees is as follows: 6 are senior management personnel, 361 are collections personnel, 159 are automobile contract origination personnel, 106 are marketing personnel (85 of whom are marketing representatives), 62 are operations and systems personnel, and 26 are administrative personnel. We believe that our relations with our employees are good. We are not a party to any collective bargaining agreement.

**MANAGEMENT**

The following table sets forth certain information with respect to our executive officers and directors as of May 31, 2006.

<b>Name</b>	<b>Age</b>	<b>Position(s) with the Company</b>
<b>Directors</b>		
Charles E. Bradley, Jr.	46	President, Chief Executive Officer, and Chairman of the Board of Directors
E. Bruce Fredrikson	68	Director
John E. McConnaughy, Jr.	77	Director
John G. Poole	63	Vice Chairman of the Board of Directors
William B. Roberts	68	Director
John C. Warner	58	Director
Daniel S. Wood	47	Director
<b>Executive Officers Who Are Not Directors</b>		
Mark A. Creatura	47	Senior Vice President, General Counsel
Jeffrey P. Fritz	46	Senior Vice President, Accounting and Chief Financial Officer
Curtis K. Powell	49	Senior Vice President, Contract Origination
Robert E. Riedl	42	Senior Vice President, Finance and Chief Investment Officer
Christopher Terry	38	Senior Vice President, Servicing

*Charles E. Bradley, Jr.* has been our President and a director since our formation in March 1991, and was elected Chairman of the Board of Directors in July 2001. In January 1992, Mr. Bradley was appointed Chief Executive Officer. From April 1989 to November 1990, he served as Chief Operating Officer of Barnard and Company, a private investment firm. From September 1987 to March 1989, Mr. Bradley, Jr. was an associate of The Harding Group, a private investment banking firm. Mr. Bradley does not currently serve on the board of directors of any other publicly-traded companies.

*E. Bruce Fredrikson* has been a director since March 2003. He is a Professor of Finance, Emeritus, at Syracuse University's Martin J. Whitman School of Management, where he taught from 1966 to 2003. Mr. Fredrikson has published numerous papers on accounting and finance topics. He is also a director of Track Data Corporation and Colonial Commercial Corp.

*John E. McConnaughy, Jr.* has been a director since 2001. He is the Chairman and Chief Executive Officer of JEMC Corporation, which is a personal holding company he formed in 1985. From 1981 to 1992 he was the Chairman and Chief Executive Officer of GEO International Corp, a company in the business of nondestructive testing, screen-printing and oil field services. Mr. McConnaughy was previously and concurrently Chairman and Chief Executive Officer of Peabody International Corp., from 1969 to 1986. He currently serves as a director of Levcor International, Inc., Wave Systems, Inc., Allis Chalmers Corp. and Arrow Resources Development Ltd. Mr. McConnaughy is also Chairman of the Board of Trustees of the Strang Clinic and is the Chairman Emeritus of the Board of the Harlem School of the Arts.

*John G. Poole* has been a director since November 1993 and our Vice Chairman since January 1996. He is now a private investor, having previously been a director and Vice President of Stanwich Partners, Inc. ( SPI ) until July 2001. SPI, which Mr. Poole co-founded in 1982, acquired controlling interests in companies in conjunction with their



existing management. Mr. Poole is also a director of Reunion Industries, Inc.

*William B. Roberts* has been a director since our formation in March 1991. Since 1981, he has been the President of Monmouth Capital Corp., an investment firm that specializes in management buyouts.

*John C. Warner* has been a director since April 2003. Mr. Warner was chief executive officer of O Neill Clothing, a manufacturer and marketer of apparel and accessories from 1996 until his retirement in May 2005.

*Daniel S. Wood* has been a director since July 2001. Mr. Wood is president of Carclo Technical Plastics, a manufacturer of custom injection moldings. Previously, from 1988 to September 2000, he was the chief operating officer and co-owner of Carrera Corporation.

*Mark A. Creatura* has been Senior Vice President General Counsel since October 1996. From October 1993 through October 1996, he was Vice President and General Counsel at Urethane Technologies, Inc., a polyurethane chemicals formulator. Mr. Creatura was previously engaged in the private practice of law with the Los Angeles law firm of Troy & Gould Professional Corporation, from October 1985 through October 1993.

*Jeffrey P. Fritz* has been Senior Vice President Chief Financial Officer since April 2006. He was Senior Vice President - Accounting from August 2004 through March 2006. He served as a consultant to us from May 2004 to August 2004. Previously, he was the Chief Financial Officer of SeaWest Financial Corp. from February 2003 to May 2004, and the Chief Financial Officer of AFCO Auto Finance from April 2002 to February 2003. He practiced public accounting with Glenn M. Gelman & Associates from March 2001 to April 2002 and was Chief Financial Officer of Credit Services Group, Inc. from May 1999 to November 2000. He previously served as our Chief Financial Officer from its inception through May 1999.

*Curtis K. Powell* has been Senior Vice President Contract Origination since June 2001. Previously, he was our Senior Vice President Marketing, from April 1995. He joined us in January 1993 as an independent marketing representative until being appointed Regional Vice President of Marketing for Southern California in November 1994. From June 1985 through January 1993, Mr. Powell was in the retail automobile sales and leasing business.

*Robert E. Riedl* has been Senior Vice President Chief Investment Officer since April 2006. Mr. Riedl was Senior Vice President Chief Financial Officer from August 2003 until assuming his current position. Mr. Riedl joined the Company as Senior Vice President Risk Management in January 2003. Previously, Mr. Riedl was a Principal at Northwest Capital Appreciation ( NCA ), a middle market private equity firm, from 2000 to 2002. For a year prior to joining Northwest Capital, Mr. Riedl served as Senior Vice President for one of NCA s portfolio companies, SLP Capital. Mr. Riedl was an investment banker for ContiFinancial Services Corporation from 1995 until joining SLP Capital in 1999.

*Christopher Terry* has been Senior Vice President Servicing since May 2005, and prior to that was Senior Vice President Asset Recovery since January 2003. He joined us in January 1995 as a loan officer, held a series of successively more responsible positions, and was promoted to Vice President Asset Recovery in June 1999. Mr. Terry was previously a branch manager with Norwest Financial from 1990 to October 1994.

**CERTAIN TRANSACTIONS**

*Levine Leichtman.* Since 1998, we have entered into a series of financing transaction with Levine Leichtman Capital Partners II, L.P., or Levine Leichtman, one of the selling shareholders, to provide us with funding in the form of sales of senior subordinated and senior secured debt securities.

As of March 31, 2006, we are indebted to Levine Leichtman in the principal amount of \$40.0 million, comprising the Term D Note, the Term E Note and the Term F Note. Such notes bear interest at 11.75% per annum, and were at that time due on various dates through December 2006, after having been previously amended from higher rates and earlier maturities.

On December 13, 2005, we agreed with Levine Leichtman to extend the maturity date of the Term D Note. As of that date, our debt to Levine Leichtman comprised four tranches, with different maturity dates. The following table sets forth the principal amount of each such tranche as of December 13, 2005, and the maturity date before and after the December 13, 2005 amendment:

<b>Term Note</b>	<b>Principal Amount</b>	<b>Date Due Prior to Amendment</b>	<b>Date Due After Amendment</b>
Term B Note	\$19,828,527	December 15, 2005	December 15, 2005
Term D Note	15,000,000	December 15, 2005	December 18, 2006
Term E Note	15,000,000	May 27, 2006	May 27, 2006
Term F Note	10,000,000	June 24, 2006	June 24, 2006

At that time, we agreed to pay Levine Leichtman a modification fee with respect to amendments to the Term D Note in the amount of \$600,000, payable in two installments of \$150,000 and \$450,000; however, if we repaid in full the Term D Note on or prior to June 14, 2006, then the modification fee would be limited to the first installment of \$150,000 (which installment we paid in December 2005). The Term D Note was not paid on or prior to June 14, 2006, and the second installment of the fee of \$450,000, which was due on July 10, 2006, was paid on that date. The due date of the Term B Note was not changed by the December 13, 2005 amendment, and the Term B Note was paid when due.

On May 26, 2006, we agreed with Levine Leichtman to extend the maturity date of the Term E and Term F Notes, in exchange for a fee of \$500,000. As of May 26, 2006, our debt to Levine Leichtman comprised three tranches, with different maturity dates. The following table sets forth the principal amount of each such tranche as of that date, and the maturity date before and after the May 26, 2006 amendment:

<b>Term Note</b>	<b>Principal Amount</b>	<b>Date Due Prior to Amendment</b>	<b>Date Due After Amendment</b>
Term D Note	\$15,000,000	December 18, 2006	December 18, 2006
Term E Note	15,000,000	May 27, 2006	May 31, 2007
Term F Note	10,000,000	June 24, 2006	May 31, 2007

All of our indebtedness owing to Levine Leichtman, as well as the guaranty obligations of our subsidiaries, is secured by a blanket security interest in favor of Levine Leichtman on substantially all of our assets and of those of our subsidiaries.

In addition to our debt obligations, Levine Leichtman holds a residual warrant to purchase 1,000 shares of our common stock for nominal consideration (which is expected to be exercised immediately prior to the sale of its shares in this offering), and has certain rights to require that we register its shares of our common stock, including those 1,000 shares issuable upon exercise of the warrant. See *The Selling Shareholders Registration Rights*.

The terms of our transactions with Levine Leichtman were determined by arm's length negotiation.

*CPS Leasing.* We hold 80% of the outstanding shares of the capital stock of CPS Leasing, Inc. ( CPSL ). The remaining 20% of CPSL is held by Charles E. Bradley, Jr., who is our President and a director of the Company. CPSL engaged in the equipment leasing business, and is currently in the process of liquidation as its leases come to term. CPSL financed its purchases of the equipment that it leases to others through either of two lines of credit. Amounts borrowed by CPSL under one of those two lines of credit have been guaranteed by us. As of December 31, 2005 both lines of credit have been paid. We have also financed the operations of CPSL by making operating

advances and by advancing to CPSL the fraction of the purchase prices of its leased equipment that CPSL did not borrow under its lines of credit. The aggregate amount of advances we made to CPSL as of March 31, 2006, is approximately \$1.1 million. The advances related to operations bear interest at the rate of 8.5% per annum. The advances related to the fraction of the purchase price of leased equipment are not interest bearing.

*Employee Indebtedness.* To assist certain officers in exercising stock options, we lent to such officers the exercise price of options such officers exercised in May and July 2002. The loans are fully secured by common stock of the Company, bear interest at 5.50% per annum and are due in 2007. Our chief executive officer (Mr. Bradley), one other executive officer (Mr. Terry), and four officers other than executive officers borrowed money on those terms and still have a balance outstanding. The highest balances of the loans for the period January 1, 2002 through April 30, 2006, were \$350,000 for Mr. Bradley and \$27,375 for one non-executive officer. Pursuant to the Sarbanes-Oxley Act of 2002, we have ceased providing any loans to our executive officers.

The agreements and transactions described above (other than our agreements and transactions with Levine Leichtman) were entered into with parties who personally benefited from such transactions and who had a control or fiduciary relationship with us. In each case such agreements and transactions have been reviewed and approved by the members of our Board of Directors who are disinterested with respect thereto.

**PRINCIPAL AND SELLING SHAREHOLDERS**

The following table sets forth information regarding beneficial ownership of our common stock by: (1) each person (including groups as that term is used in Section 13(d)(3) of the Exchange Act) we know to be a beneficial owner of more than five percent of our common stock, (2) each our directors and named executive officers, (3) all of our directors and named executive officers as a group, and (4) each of the selling shareholders in this offering. This information is presented as of June 30, 2006 and as adjusted to reflect the sale of the common stock in this offering. Other than with respect to our directors and executive officers, this information is based on reports filed with the SEC by the persons listed in the table below. If you wish, you may obtain a copy of these reports from the SEC. Except as otherwise indicated, and subject to applicable community property and similar laws, each of the persons named has sole voting and investment power with respect to the shares shown as beneficially owned by such persons. Except as otherwise noted, the address of each person named is c/o Consumer Portfolio Services, Inc., 16355 Laguna Canyon Road, Irvine, CA 92618.

Beneficial ownership is a technical term broadly defined by the SEC to mean more than direct ownership. A person has beneficial ownership of a share not only if he or she owns the share in the usual sense, but also if he or she has the power to vote, sell or otherwise dispose of the share. In computing the number of shares of common stock beneficially owned by a person and the percentage ownership of that person, shares of common stock that are subject to options or warrants held by that person that are exercisable within 60 days of June 30, 2006 are deemed outstanding. These shares are not, however, deemed outstanding for the purpose of computing the percentage ownership of any other person.

Name and Address of Beneficial Owner	Actual		To Be Sold in This Offering (2)	As Adjusted (1)	
	Amount and Nature of Beneficial Ownership (2)	Percent of Class		Amount and Nature of Beneficial Ownership	Percent of Class (1)
Charles E. Bradley, Jr.	3,226,990 (3)	14.1 %		3,226,990	13.8 %
E. Bruce Fredrikson	61,000	0.3 %		61,000	0.3 %
John E. McConaughy, Jr.	10,000	0.0 %		10,000	0.0 %
John G. Poole	699,693	3.2 %		699,693	3.1 %
William B. Roberts	864,107	4.0 %		864,107	3.9 %
John C. Warner	60,000	0.3 %		60,000	0.3 %
Daniel S. Wood	80,000	0.4 %		80,000	0.4 %
Jeffrey P. Fritz	180,000	0.8 %		180,000	0.8 %
Curtis K. Powell	306,262	1.4 %		306,262	1.4 %
Robert E. Riedl	237,008	1.1 %		237,008	1.1 %
Christopher Terry	221,076	1.0 %		221,076	1.0 %
All directors and executive officers combined (12 persons)	6,193,775 (4)	25.8 %		6,193,775	25.3 %
Levine Leichtman Capital Partners II, L.P., 335 North Maple Drive, Suite 240,	3,987,558 (5)	18.3 %	3,500,000	487,558 (6)	2.2 %

Beverly Hills, CA 90210

LC Capital Master Fund, c/o

Lampe Conway & Co LLC,

730 Fifth Avenue Suite

1002, New York NY 10019

1,126,915

5.2 %

1,126,915

5.1 %

Stanwich Financial Services

Corp.,

170 Mason Street,

Greenwich, CT 06830

546,959

2.5 %

500,000 46,959 (7)

0.2 %

(1)

Based on the sale of 4,000,000 shares by the selling shareholders and 500,000 shares by us.

(2)

Includes certain shares that may be acquired from us within 60 days after June 30, 2006 upon exercise of options, as follows: Mr. Bradley, Jr., 1,136,099 shares; Mr. Fredrikson, 60,000 shares; Mr. McConnaughy, 10,000 shares; Mr. Poole, 30,000 shares; Mr. Roberts, 30,000 shares; Mr. Warner, 60,000 shares; Mr. Wood, 40,000 shares; Mr. Fritz, 180,000 shares; Mr. Powell, 125,000 shares; Mr. Riedl, 235,000 shares; and Mr. Terry, 178,500 shares. The calculation of beneficial ownership also includes, in the case of the executive officers, an approximate number of shares each executive officer could be deemed to hold through contributions made to our Employee 401(k) Plan (the 401(k) Plan ). The 401(k) Plan provides an option for all participating employees to indirectly purchase our common stock through buying units in a mutual fund. Each unit in the mutual fund represents an interest in our common stock, cash and cash equivalents.

(3)

Includes 271,540 shares held by trusts of which Mr. Bradley is the co-trustee, and as to which shares Mr. Bradley has shared voting and investment power. The co-trustee, who has shared voting and investment power as to all such shares (representing 1.25% of beneficial ownership), is Kimball Bradley, whose address is 11 Stanwix Street, Pittsburgh, PA 15222.

(4)

Includes 2,219,599 shares that may be acquired within 60 days after June 30, 2006, upon exercise of options and conversion of convertible securities.

(5)

Comprises 3,986,558 issued shares and 1,000 shares that are issuable upon exercise of an outstanding warrant.

(6)

If the underwriter's overallotment option were exercised in full, Levine Leichtman would sell all of its 3,987,558 shares, and hold no shares after the offering.

(7)

If the underwriter's overallotment option were exercised in full, Stanwix would sell all of its 546,959 shares, and hold no shares after the offering.

## DESCRIPTION OF CAPITAL STOCK

### General

We are authorized to issue 30,000,000 shares of common stock, no par value and 10,000,000 shares of preferred stock, \$1.00 par value per share. As of June 30, 2006, there were 21,799,322 shares of our common stock outstanding and no shares of our preferred stock outstanding.

### Common Stock

Holders of our common stock are entitled to one vote per share on all matters to be voted upon by our shareholders, including the election of directors. Holders of our common stock are entitled to cumulate their votes in the election of directors if they comply with the provisions of our Bylaws as to cumulative voting. In cumulative voting, each holder is permitted to cast such number of votes in the aggregate as equals the number of shares of stock held multiplied by the number of directors to be elected. The holders may cast the whole number of such votes for one nominee for director or distribute the votes among two or more nominees as the holder sees fit.

Holders of our common stock are entitled to receive such dividends as may be declared from time to time by our Board of Directors out of funds legally available therefore, subject to significant contractual restrictions. For more information, see Dividend Policy. In the event of our liquidation, dissolution or winding up, holders of common stock are entitled to share ratably in all assets remaining after payment of liabilities and after satisfaction of the liquidation preference of any outstanding preferred stock. Holders of our common stock have no preemptive, conversion or redemption rights and are not subject to further assessments by us. All of the currently outstanding shares of our common stock are fully paid and nonassessable.



The transfer agent and registrar for our common stock is American Stock Transfer & Trust Company.

**Preferred Stock**

Our articles of incorporation provide that we are authorized to issue up to 10,000,000 shares of preferred stock, with such designations, rights and preferences as may be determined from time to time by the Board of Directors. Accordingly, the Board of Directors is empowered, without shareholder approval, to issue preferred stock with dividend, liquidation, conversion, voting or other rights which could adversely affect the voting power or other rights of the holders of the our common stock. In the event of issuance, the preferred stock could be utilized, under certain circumstances, as a method of discouraging, delaying or preventing a change in control of the company. As of June 30, 2006, we have no shares of preferred stock outstanding, and no present intentions to issue any shares of preferred stock.

## SELLING SHAREHOLDERS

### General

This is an offering of our common stock primarily by the selling shareholders, consisting of Levine Leichtman Capital Partners II, L.P., one of our principal shareholders, and Stanwich Financial Services Corp. We agreed to register the shares being offered by the selling shareholders pursuant to certain registration rights agreements we entered into with each of them. We have agreed with the selling shareholders to register their shares of our common stock offered by this prospectus through an underwritten offering. For more information, see Registration Rights Agreements.

### Levine Leichtman Capital Partners II, L.P.

Levine Leichtman Capital Partners II, L.P., or Levine Leichtman, is one of our principal shareholders, and beneficially owned approximately 18.3% of the outstanding shares of our common stock as of June 30, 2006. Levine Leichtman was formed in 1997 and acquired its shares of our common stock in connection with a series of purchases of our senior subordinated and senior secured debt securities beginning in October 1998. Certain of these debt securities were issued together with warrants that allowed Levine Leichtman to purchase shares of our common stock at a nominal consideration. As of June 30, 2006, Levine Leichtman also holds \$40.0 million of our outstanding secured senior debt securities. For more information, see Certain Transactions. Levine Leichtman also holds a warrant exercisable to purchase 1,000 shares of our common stock, which it intends to exercise immediately prior to the closing of this offering.

Levine Leichtman is offering 3,500,000 shares of our common stock and has granted the underwriter a 30-day option to purchase up to an additional 487,558 shares of our common stock to cover over-allotments, as described in

Underwriting. Upon successful completion of this offering and the full exercise of the over-allotment option, Levine Leichtman will no longer have any beneficial ownership of our common stock.

### Stanwich Financial Services Corp.

Stanwich Financial Services Corp., or Stanwich, an entity in liquidation, beneficially owned approximately 2.5% of the outstanding shares of our common stock as of June 30, 2006. Stanwich acquired 443,459 of its shares of our common stock from us in July 1998 in a private transaction and 103,500 of its shares of our common stock from us in March 2000 in connection with the restructuring of then existing debt financing provided to us by Stanwich. During June 2004, we completed repayment of all of our debt obligations to Stanwich.

Stanwich is offering 500,000 shares of our common stock and has granted the underwriter a 30-day option to purchase up to an additional 46,959 shares of our common stock to cover over-allotments, as described in Underwriting. Upon successful completion of this offering and the full exercise of the over-allotment option, Stanwich will no longer have any beneficial ownership of our common stock.

### Registration Rights Agreements

#### *Levine Leichtman Capital Partners II, L.P.*

We entered into a registration rights agreement with Levine Leichtman in connection with its initial investment in us in 1998. The terms of that agreement have subsequently been amended and restated. Under that registration rights agreement, as subsequently amended and restated, we agreed to register the common stock offered by Levine Leichtman in this prospectus through an underwritten offering. In addition, if less than all of Levine Leichtman's shares are sold in this offering, we will have an obligation to register such remaining shares at their request. We also agreed that if we propose to register any securities in connection with the public offering of such securities solely for

cash, then we will give Levine Leichtman the ability to participate in the registration. However, we will not have the obligation to provide such piggy-back registration rights if the registration we are proposing to undertake is:

on Form S-4, Form S-8 or any successor form that may be adopted by the SEC, or with respect to an employee benefit plan;

for an exchange offer solely to our existing shareholders; or

with respect to a dividend reinvestment plan.

Our obligations under the registration rights agreement to effectuate a demand registration will terminate on the earlier to occur of:

five years after repayment of all of our indebtedness to Levine Leichtman; or

the date on which less than five percent of our outstanding shares of common stock are held by Levine Leichtman.

***Stanwich Financial Services Corp.***

We entered into a registration rights agreement with Stanwich in connection with debt financing provided by Stanwich in June 1997. We entered into a second registration rights agreement with Stanwich in July 1998 in connection with Stanwich's purchase of shares of our common stock in a private transaction. These agreements were amended and consolidated in connection with the restructuring of certain debt financing provided to us by Stanwich and certain affiliated parties in November 1998. Under that consolidated registration rights agreement, we agreed to register the common stock offered by Stanwich in this prospectus through an underwritten offering. In addition, if less than all of Stanwich's shares are sold in this offering, we will have an obligation to register such remaining shares at their request. We also agreed that if we propose to register any securities in connection with the public offering of such securities solely for cash, then we will give Stanwich the ability to participate in the registration, subject to the same exceptions as exist in Levine Leichtman's registration rights agreement.

## UNDERWRITING

We and the selling shareholders have entered into an underwriting agreement with the underwriter, JMP Securities LLC, and subject to the terms and conditions contained in the underwriting agreement, we and the selling shareholders have agreed to sell to the underwriter, and the underwriter has agreed to purchase from us and the selling shareholders 4,500,000 shares of our common stock.

The underwriting agreement provides that the underwriter's obligation to pay for and accept delivery of our common stock is subject to approval of various legal matters by its counsel and to other conditions. The underwriter is obligated to take and pay for all shares of our common stock offered if any of the shares are taken, other than those covered by the over-allotment option described below.

The underwriter proposes to offer shares of our common stock directly to the public at the public offering price per share listed on the cover page of this prospectus and to selected dealers at this price less a concession not in excess of \$ \_\_\_\_\_ per share, of which \$ \_\_\_\_\_ per share may be reallocated to other dealers. After this offering, the public offering price, concession and reallocation to dealers may be reduced by the underwriter. No such reduction shall change the amount of proceeds to be received by us and by the selling shareholders as listed on the cover page of this prospectus. The common stock is offered by the underwriter, subject to receipt and acceptance by the underwriter and subject to the underwriter's right to reject any order in whole or in part.

### Over-Allotment Option

We and the selling shareholders have granted the underwriter an option, exercisable for 30 days after the date of this prospectus, to purchase up to an additional 675,000 shares of common stock to cover over-allotments, if any, at the public offering price less the underwriting discounts and commissions listed on the cover page of this prospectus. If the underwriter exercises the option to purchase any of the 675,000 additional shares of common stock, they will have a firm commitment, subject to a number of conditions, to purchase these shares. If purchased, these additional shares will be sold by the underwriter on the same terms as those on which the shares offered hereby are being sold. We and the selling shareholders will be obligated, pursuant to the over-allotment option, to sell shares to the underwriter to the extent the over-allotment option is exercised. The underwriter may exercise the over-allotment option only to cover over-allotments made in connection with the sale of the shares of common stock offered in this offering.

### Discounts and Commissions

The following table shows the per share and total underwriting discount that we and the selling shareholders will pay to the underwriter. The total amounts are shown assuming both no exercise and full exercise of the over-allotment option to purchase 675,000 additional shares of our common stock, if any.

	Per share	Total	
		No Exercise of Option	Full Exercise of Option
Underwriting discounts and commissions payable by us	\$	\$	\$
Underwriting discounts and commissions payable by the selling shareholders	\$	\$	\$

We estimate fees and expenses payable by us in connection with this offering, other than the underwriting discounts and commissions referred to above, will be approximately \$170,000, including fees and expenses paid by us on behalf of the selling shareholder.

### Indemnity

We and the selling shareholders have agreed to indemnify the underwriter against particular liabilities, including certain liabilities under the Securities Act, or to contribute to payments the underwriter may be required to make in respect thereof.

## **Lock-Up Agreements**

We have agreed with JMP Securities LLC, subject to particular exceptions, that we will not, without the prior written consent of JMP Securities LLC, directly or indirectly sell, offer, contract or grant any option to sell, pledge, transfer, or establish an open put equivalent position within the meaning of Rule 16a-1(h) of the Exchange Act, or otherwise dispose of or enter into any transaction which may result in the disposition of any shares of our common stock or securities convertible into, exchangeable or exercisable for any shares of our common stock for a period of 90 days after the date of this prospectus.

Each of our executive officers and directors has agreed with JMP Securities LLC not to directly or indirectly sell, offer, contract, grant or transfer any option to sell, transfer, or establish an open put equivalent position within the meaning of Rule 16a-1(h) of the Exchange Act, or otherwise dispose of any shares of our common stock or securities convertible into, exchangeable or exercisable for any shares of our common stock, or publicly disclose the intention to make any offer, sale, grant, transfer or disposition without the prior written consent of JMP Securities LLC for a period of 90 days after the date of this prospectus.

If the over-allotment option is fully exercised, the selling shareholders will no longer hold any shares of our common stock. In the event that the selling shareholders retain any shares of our common stock upon completion of this offering, each of the selling shareholders has agreed with JMP Securities LLC not to directly or indirectly sell, offer, contract, grant or transfer any option to sell, transfer, or establish an open put equivalent position within the meaning of Rule 16a-1(h) of the Exchange Act, or otherwise dispose of any shares of our common stock or securities convertible into, exchangeable or exercisable for any shares of our common stock, or publicly disclose the intention to make any offer, sale, grant, transfer or disposition without the prior written consent of JMP Securities LLC for a period of 90 days after the date of this prospectus. If prior to the closing of this offering, Levine Leichtman provides the underwriter with written notice that it will not participate in the offering, then from and after the date of such notice, Levine Leichtman will no longer be subject to such restrictions pursuant to the lock-up agreement. If prior to the closing of this offering, Stanwich provides the underwriter with written notice that it will not participate in the offering, then Stanwich would be subject to restrictions set forth in the lock-up agreement for a period of 30 days after the date of this prospectus.

## **Listing**

Our common stock is listed on the Nasdaq National Market under the symbol CPSS.

## **Stabilization**

In connection with this offering, the underwriter is permitted to engage in certain transactions that stabilize the price of our common stock. These transactions consist of bids or purchases for the purpose of pegging, fixing or maintaining the price of our common stock. If the underwriter creates a short position in our common stock in connection with this offering by selling more than 675,000 shares of common stock, it may reduce that short position by purchasing our common stock in the open market. In general, purchases of a security for the purpose of stabilization or to reduce a short position could cause the price of the security to be higher than it might be in the absence of those purchases. Neither we, the selling shareholders, nor the underwriter make any representation or prediction as to the direction or magnitude of any effect that the transactions described above may have on the price of our common stock. In addition, neither we, the selling shareholders, nor the underwriter make any representation that the underwriter will engage in those transactions or that those transactions, once commenced, will not be discontinued without notice.

## **Electronic Distribution**

A prospectus in electronic format may be made available on the Internet sites or through other online services maintained by the underwriter and/or selling group members, if any, participating in the offering, or by their affiliates. In those cases, prospective investors may view offering terms online and, depending upon the particular underwriter or selling group member, prospective investors may be allowed to place orders online. Other than the prospectus in electronic format, the information on the underwriter's or any selling group member's website and any information contained in any other website maintained by the underwriter or any selling group member is not part of the prospectus or the registration statement of which this prospectus forms a part, has not been approved and/or



endorsed by us or the underwriter or any selling group member in its capacity as underwriter or selling group member and should not be relied upon by investors.

### **Other Agreements**

JMP Securities LLC and its affiliates may provide us with investment banking, financial advisory, or commercial banking services in the future, for which it may receive customary compensation.

### **LEGAL MATTERS**

The validity of the common stock will be passed upon by Andrews Kurth, LLP, Dallas, Texas. Legal matters in connection with this offering will be passed upon for the underwriter by Kirkpatrick & Lockhart Nicholson Graham LLP, Los Angeles, California.

### **EXPERTS**

The consolidated financial statements of Consumer Portfolio Services, Inc. as of and for the years ended December 31, 2004 and 2005 have been incorporated by reference herein in reliance upon the report of McGladrey & Pullen LLP, independent registered public accountants, incorporated by reference herein, and upon the authority of said firm as experts in accounting and auditing.

The consolidated financial statements of Consumer Portfolio Services, Inc. for the year ended December 31, 2003, have been incorporated by reference herein in reliance upon the report of KPMG LLP, independent registered public accounting firm, incorporated by reference herein, and upon the authority of said firm as experts in accounting and auditing.

### **WHERE YOU CAN FIND MORE INFORMATION**

We file annual, quarterly and current reports and proxy statements and other information with the SEC. You may read and copy any document which we file at the SEC's public reference room located at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference rooms. Our filings with the SEC are also available to the public over the Internet at a website maintained by the SEC at <http://www.sec.gov>.

We have filed with the SEC a registration statement on Form S-3 under the Securities Act with respect to the common stock offered hereby. This prospectus is a part of that registration statement. This prospectus does not contain all the information set forth in the registration statement or in the exhibits to the registration statement, certain portions of which have been omitted as permitted by the rules and regulations of the SEC. For further information with respect to us and the securities offered hereby, reference is made to the registration statement and the exhibits and the financial statements, notes and schedules filed as part thereof or incorporated by reference therein, which may be inspected as described above. Statements made in this prospectus concerning the contents of any documents referred to in this prospectus are not necessarily complete, and in each instance are qualified in all respects by reference to the copy of the document filed as an exhibit to the registration statement of which this prospectus is a part.

### **DOCUMENTS INCORPORATED BY REFERENCE**

The SEC allows us to incorporate by reference information in documents that we file with it. We have elected to use a similar procedure in connection with this prospectus, which means that we can disclose important information to you by referring you to another document filed separately with the SEC. The information incorporated by reference is considered to be a part of this prospectus, and information that we file later with the SEC will automatically update and supersede this information. We incorporate by reference the documents listed below and, from the date of this

prospectus, any future filings made by us with the SEC which we may make under Sections 13(a), 13(c), 14 or 15(d) of the Exchange Act (other than information in listed documents and future filings that is deemed not to be filed):

- 

Annual Report on Form 10-K for the year ended December 31, 2005;

- Quarterly Report on Form 10-Q for the quarter ended March 31, 2006; and

- Current Reports on Form 8-K filed on January 5, March 7, April 4, April 24, June 2, June 30, and July 7, 2006.

Any statement contained in this prospectus or in a document incorporated or deemed to be incorporated by reference herein will be deemed to be modified or superseded for purposes of this prospectus to the extent that a statement contained in any subsequently filed document which is or is deemed to be incorporated by reference herein modifies or supersedes such statement. Any such statement so modified or superseded will not be deemed, except as so modified or superseded, to constitute a part of this prospectus.

You may request a copy of these incorporated filings, without charge, other than exhibits to such documents unless such exhibits are specifically incorporated by reference in the document that this prospectus incorporates. You may request copies by writing or telephoning Consumer Portfolio Services, Inc., 16355 Laguna Canyon Rd., Irvine, California 92618, Attention: Corporate Secretary, telephone (949) 753-6800. You may also obtain copies of some of these documents at our website at <http://www.consumerportfolio.com>. Information included or referenced to on our website is not part of this prospectus.

**INDEX TO FINANCIAL STATEMENTS**

**Annual Consolidated Financial Statements**

	<b>Page Reference</b>
Report of Independent Registered Public Accounting Firm McGladrey & Pullen, LLP	F-2
Report of Independent Registered Public Accounting Firm KPMG LLP	F-3
Consolidated Balance Sheets as of December 31, 2005 and 2004	F-4
Consolidated Statements of Operations for the years ended December 31, 2005, 2004, and 2003	F-5
Consolidated Statements of Comprehensive Income (Loss) for the years ended December 31, 2005, 2004, and 2003	F-6
Consolidated Statements of Shareholders Equity for the years ended December 31, 2005, 2004, and 2003	F-7
Consolidated Statements of Cash Flows for the years ended December 31, 2005, 2004, and 2003	F-8
Notes to Consolidated Financial Statements for the years ended December 31, 2005, 2004, and 2003	F-10

**First Quarter Condensed Financial Statements**

	<b>Page Reference</b>
Condensed Consolidated Balance Sheets as of March 31, 2006 and December 31, 2005	F-41
Condensed Consolidated Statements of Operations for the three month periods ended March 31, 2006 and March 31, 2005	F-42
Condensed Consolidated Statements of Cash Flows for the three months ended March 31, 2006 and 2005	F-43
Notes to Condensed Consolidated Financial Statements	F-44

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors  
Consumer Portfolio Services, Inc.:

We have audited the consolidated balance sheets of Consumer Portfolio Services, Inc. and subsidiaries (the Company ) as of December 31, 2005 and 2004, and the related consolidated statements of operations, comprehensive income (loss), shareholders' equity, and cash flows for each of the two years in the period ended December 31, 2005. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Consumer Portfolio Services, Inc. and subsidiaries as of December 31, 2005 and 2004, and the results of their operations and their cash flows for each of the two years in the period ended December 31, 2005, in conformity with U.S. generally accepted accounting principles.

/s/ McGladrey & Pullen, LLP

Irvine, California  
February 24, 2006

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Board of Directors  
Consumer Portfolio Services, Inc.:

We have audited the accompanying consolidated statements of operations, comprehensive income (loss), shareholders equity, and cash flows of Consumer Portfolio Services, Inc. and subsidiaries (the Company ) for the year ended December 31, 2003. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the results of operations and cash flows of Consumer Portfolio Services, Inc. and subsidiaries for the year ended December 31, 2003, in conformity with U.S. generally accepted accounting principles.

/s/ KPMG LLP

Orange County, California  
March 15, 2004

**CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS**

	<b>December 31,</b>	
(in thousands, except share and per share data)	<b>2005</b>	<b>2004</b>
<b>Assets</b>		
Cash and cash equivalents	\$ 17,789	\$ 14,366
Restricted cash and equivalents	157,662	125,113
Finance receivables	971,304	592,806
Less: Allowance for finance credit losses	(57,728 )	(42,615 )
Finance receivables, net	913,576	550,191
Residual interest in securitizations	25,220	50,430
Furniture and equipment, net	1,079	1,567
Deferred financing costs	8,596	5,096
Deferred tax assets, net	7,532	
Accrued interest receivable	10,930	6,411
Other assets	12,760	13,425
	\$ 1,155,144	\$ 766,599
<b>Liabilities and Shareholders Equity</b>		
<b>Liabilities</b>		
Accounts payable and accrued expenses	\$ 19,568	\$ 18,153
Warehouse lines of credit	35,350	34,279
Tax liabilities, net		2,978
Notes payable	211	1,421
Residual interest financing	43,745	22,204
Securitization trust debt	924,026	542,815
Senior secured debt, related party	40,000	59,829
Subordinated renewable notes	4,655	
Subordinated debt	14,000	15,000
	1,081,555	696,679
<b>Commitments and Contingencies</b>		
<b>Shareholders equity</b>		
Preferred stock, \$1 par value; authorized 5,000,000 shares; none issued		
Series A preferred stock, \$1 par value; authorized 5,000,000 shares; 3,415,000 shares issued; none outstanding		
Common stock, no par value; authorized 30,000,000 shares; 21,687,584 and 21,471,478 shares issued and outstanding at December 31, 2005 and December 31, 2004, respectively	66,748	66,283

Additional paid in capital, warrants	794	
Retained earnings		
	8,476	5,104
Accumulated other comprehensive loss	(2,429 )	(1,017 )
Deferred compensation		(450 )
	73,589	69,920
	\$ 1,155,144	\$ 766,599

**See accompanying Notes to Consolidated Financial Statements.**

F-4

---



**CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS****Year Ended December 31,**

(in thousands, except share and per share data)

	<b>2005</b>	<b>2004</b>	<b>2003</b>
<b>Revenues:</b>			
Net gain on sale of contracts	\$	\$	\$ 10,421
Interest income	171,834	105,818	58,164
Servicing fees	6,647	12,480	17,058
Other income	15,216	14,394	19,343
	193,697	132,692	104,986
<b>Expenses:</b>			
Employee costs	40,384	38,173	37,141
General and administrative	23,095	21,293	21,271
Interest	44,148	25,876	17,867
Interest, related party	7,521	6,271	5,994
Provision for credit losses	58,987	32,574	11,390
Impairment loss on residual asset		11,750	4,052
Marketing	12,000	8,338	5,380
Occupancy	3,400	3,520	3,930
Depreciation and amortization	790	785	1,000
	190,325	148,580	108,025
Income (loss) before income tax benefit	3,372	(15,888 )	(3,039 )
Income tax benefit			(3,434 )
Net income (loss)	\$ 3,372	\$ (15,888 )	\$ 395
<b>Earnings (loss) per share:</b>			
Basic	\$ 0.16	\$ (0.75 )	\$ 0.02
Diluted	0.14	(0.75 )	0.02
<b>Number of shares used in computing earnings (loss) per share:</b>			
Basic	21,627	21,111	20,263
Diluted	23,513	21,111	21,578

**See accompanying Notes to Consolidated Financial Statements.**



**CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**

(in thousands)	Year Ended December 31,		
	2005	2004	2003
Net income (loss)	\$ 3,372	\$ (15,888 )	\$ 395
Other comprehensive income (loss):			
Minimum pension liability, net of tax	(1,412 )	1,409	(832 )
Comprehensive income (loss)	\$ 1,960	\$ (14,479 )	\$ (437 )

**See accompanying Notes to Consolidated Financial Statements.**

**CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY**

(in thousands)	<b>Common Stock</b>		<b>Additional Paid-in Capital, Warrants</b>	<b>Retained Earnings</b>	<b>Accumulated Other Comprehensive Loss</b>	<b>Deferred Compensation</b>	<b>Total</b>
	<b>Shares</b>	<b>Amount</b>					
Balance at December 31, 2002	20,528	\$ 63,929	\$	\$ 20,597	\$ (1,594 )	\$ (358 )	\$ 82,574
Common stock issued upon exercise of options, including tax benefit	609	974					974
Purchase of common stock	(548 )	(1,195 )					(1,195 )
Pension benefit obligation					(832 )		(832 )
Repurchase of warrants issued		(896 )					(896 )
Deferred compensation on stock options		1,585				(1,585 )	
Amortization of stock compensation						1,140	1,140
Net income				395			395
Balance at December 31, 2003	20,589	64,397		20,992	(2,426 )	(803 )	82,160
Common stock issued upon exercise of options, including tax benefit	575	1,079					1,079
Common stock issued upon conversion of debt	333	1,000					1,000
Purchase of common stock	(26 )	(111 )					(111 )
Pension benefit obligation					1,409		1,409

Deferred compensation on stock options		(82 )				82	
Amortization of stock compensation						271	271
Net loss				(15,888 )			(15,888 )
Balance at December 31, 2004	21,471	66,283		5,104	(1,017 )	(450 )	69,920
Common stock issued upon exercise of options, including tax benefit	415	1,311					1,311
Purchase of common stock	(199 )	(1,040 )					(1,040 )
Pension benefit obligation					(1,412 )		(1,412 )
Valuation of warrants issued			794				794
Deferred compensation on stock options		194				(194 )	
Amortization of stock compensation						644	644
Net income				3,372			3,372
Balance at December 31, 2005	21,687	\$ 66,748	\$ 794	\$ 8,476	\$ (2,429 )	\$	\$ 73,589

**See accompanying Notes to Consolidated Financial Statements.**

## CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS

	<b>Year Ended December 31,</b>		
	<b>2005</b>	<b>2004</b>	<b>2003</b>
Cash flows from operating activities:			
Net income (loss)	\$ 3,372	\$ (15,888 )	\$ 395
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Reversal of restructuring accrual		(1,287 )	
Impairment loss on residual asset		11,750	4,052
Amortization of deferred acquisition fees	(10,851 )	(6,725 )	(870 )
Amortization of discount on Class B Notes	1,486	588	
Depreciation and amortization	790	785	1,000
Amortization of deferred financing costs	3,296	3,479	2,695
Provision for credit losses	58,987	32,574	11,916
Gain of sale of Contracts, NIR			(4,381 )
Deferred compensation	644	271	1,140
Releases of cash from Trusts to Company	23,074	21,357	25,934
Initial deposits to Trusts			(18,736 )
Net deposits to Trusts to increase Credit Enhancement		(2,858 )	(20,867 )
Interest income on residual assets	(5,338 )	(4,633 )	(16,178 )
Cash received from residual interest in securitizations	30,548	54,154	45,644
Impairment charge against non-auto finance receivable assets	1,882		
Changes in assets and liabilities:			
Payments on restructuring accrual	(1,425 )	(1,969 )	(1,804 )
Restricted cash and equivalents	(55,623 )	(76,336 )	(30,641 )
Purchases of contracts held for sale			(182,045 )
Proceeds received on Contracts held for sale			283,423
Other assets	(5,578 )	(5,415 )	6,936
Deferred tax assets, net	(7,532 )		
Accounts payable and accrued expenses	1,928	715	(1,559 )
Tax liabilities	(2,978 )	(606 )	(7,162 )
Net cash provided by operating activities	36,682	9,956	98,892
Cash flows from investing activities:			
Purchases of finance receivables held for investment	(691,252 )	(505,977 )	(175,275 )
Purchases of note receivable		(2,799 )	
Proceeds received on finance receivables held for investment	279,730	196,126	6,611
Purchase of furniture and equipment	(166 )	(1,408 )	(93 )
Purchase of subsidiary, net of cash acquired			(10,181 )
Net cash used in investing activities	(411,688 )	(314,058 )	(178,938 )

## Cash flows from financing activities:

Proceeds from issuance of residual financing debt	45,800	44,000	
Proceeds from issuance of securitization trust debt	662,350	474,720	154,375
Proceeds from issuance of senior secured debt, related party		25,000	25,000
Proceeds from issuance of subordinated renewable notes	4,685		
Net proceeds from warehouse lines of credit	1,071	570	31,332
Repayment of residual interest financing debt	(24,259 )	(21,796 )	
Repayment of securitization trust debt	(282,625 )	(177,611 )	(96,484 )
Repayment of senior secured debt, related party	(19,829 )	(15,137 )	(25,107 )
Repayment of subordinated debt and renewable notes	(1,030 )	(20,000 )	(1,000 )
Repayment of notes payable	(1,209 )	(1,909 )	(3,748 )
Repayment of related party debt		(16,500 )	
Payment of financing costs	(6,796 )	(7,046 )	(2,553 )
Repurchase of common stock	(1,040 )	(111 )	(1,195 )
Repurchase of warrants issued			(896 )
Exercise of options and warrants	1,311	1,079	584
Net cash provided by financing activities	378,429	285,259	80,308

**CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS**

	<b>Year Ended December 31,</b>		
	<b>2005</b>	<b>2004</b>	<b>2003</b>
Increase (decrease) in cash and cash equivalents	3,423	(18,843 )	262
Cash and cash equivalents at beginning of period	14,366	33,209	32,947
Cash and cash equivalents at end of period	\$ 17,789	\$ 14,366	\$ 33,209
Supplemental disclosure of cash flow information:			
Cash paid (received) during the period for:			
Interest	\$ 45,929	\$ 28,228	18,677
Income taxes	9,377	420	3,728
Supplemental disclosure of non-cash investing and financing activities:			
Stock-based compensation	\$ 644	\$ 271	1,140
Conversion of related party debt to common stock		(1,000 )	
Pension benefit obligation, net	1,412	(1,409 )	832
Value of warrants issued	794		

**See accompanying Notes to Consolidated Financial Statements.**



**CONSUMER PORTFOLIO SERVICES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(1) Summary of Significant Accounting Policies**

**Description of Business**

Consumer Portfolio Services, Inc. ( CPS ) was incorporated in California on March 8, 1991. CPS and its subsidiaries (collectively, the Company ) specialize in purchasing, selling and servicing retail automobile installment sale contracts ( Contracts ) originated by licensed motor vehicle dealers ( Dealers ) located throughout the United States. Dealers located in Texas, California, Ohio and Florida represented 10.7%, 9.0%, 7.5% and 7.1%, respectively of Contracts purchased during 2005 compared with 12.1%, 8.6%, 5.1% and 6.1%, respectively in 2004. No other state had a concentration in excess of 7.0%. The Company specializes in Contracts with obligors who generally would not be expected to qualify for traditional financing, such as that provided by commercial banks or automobile manufacturers captive finance companies.

The Company is subject to various regulations and laws as they relate to the extension of credit in consumer credit transactions. Although the Company believes it is currently in material compliance with these regulation and laws, there can be no assurance that the Company will be able to maintain such compliance. Failure to comply with such laws and regulations could have a material adverse effect on the Company.

**Acquisitions**

On March 8, 2002, the Company acquired MFN Financial Corporation and its subsidiaries in a merger (the MFN Merger ). On May 20, 2003, the Company acquired TFC Enterprises, Inc. and its subsidiaries in a second merger (the TFC Merger ). Each merger was accounted for as a purchase. MFN Financial Corporation and its subsidiaries ( MFN ) and TFC Enterprises, Inc. and its subsidiaries ( TFC ) were engaged in businesses similar to that of the Company: buying Contracts from Dealers, financing those Contracts through securitization transactions, and servicing those Contracts. MFN ceased acquiring Contracts in March 2002; TFC continues to acquire Contracts under its TFC Programs.

On April 2, 2004, the Company purchased a portfolio of Contracts and certain other assets (the SeaWest Asset Acquisition ) from SeaWest Financial Corporation ( SeaWest ). In addition, the Company was named the successor servicer for three term securitization transactions originally sponsored by SeaWest (the SeaWest Third Party Portfolio ). The Company does not intend to offer financing programs similar to those previously offered by SeaWest.

**Principles of Consolidation**

The Consolidated Financial Statements include the accounts of Consumer Portfolio Services, Inc. and its wholly-owned subsidiaries, certain of which are Special Purpose Subsidiaries ( SPS ), formed to accommodate the structures under which the Company purchases and securitizes its Contracts. The Consolidated Financial Statements also include the accounts of CPS Leasing, Inc., an 80% owned subsidiary. All significant intercompany balances and transactions have been eliminated in consolidation.

**Cash and Cash Equivalents**

For purposes of the statements of cash flows, the Company considers all highly liquid debt instruments with original maturities of three months or less to be cash equivalents. Cash equivalents consist of cash on hand and due from banks and money market accounts. The Company's cash is primarily deposited at three financial institutions. The Company maintains cash due from banks in excess of the bank's insured deposit limits. The Company does not believe it is

exposed to any significant credit risk on these deposits. As part of certain financial covenants related to debt facilities, the Company is required to maintain a minimum unrestricted cash balance.

F-10

---

**CONSUMER PORTFOLIO SERVICES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Finance Receivables, net of unearned income**

Finance receivables are presented at cost. All Finance receivable Contracts are held for investment and include automobile installment sales contracts on which interest is pre-computed and added to the amount financed. The interest on such Contracts is included in unearned finance charges. Unearned finance charges are amortized using the interest method over the contractual term of the receivables. Generally, payments received on finance receivables are restricted to certain securitized pools, and the related Contracts cannot be resold. Finance receivables are charged off pursuant to the controlling documents of certain securitized pools, generally before they become contractually delinquent five payments. Contracts that are deemed uncollectible prior to the maximum delinquency period are charged off immediately. Management may authorize an extension of payment terms if collection appears likely during the next calendar month.

The Company's portfolio of finance receivables is comprised of smaller-balance homogeneous Contracts that are collectively evaluated for impairment on a portfolio basis. The Company reports delinquency on a contractual basis. Once a Contract becomes greater than 90 days delinquent, the Company does not recognize additional interest income until the borrower under the Contract makes sufficient payments to be less than 90 days delinquent. Any payments received by a borrower that is greater than 90 days delinquent is first applied to accrued interest and then to principal reduction.

**Allowance for Finance Credit Losses**

In order to estimate an appropriate allowance for losses to be incurred on finance receivables, the Company uses a loss allowance methodology commonly referred to as static pooling, which stratifies its finance receivable portfolio into separately identified pools. Using analytical and formula driven techniques, the Company estimates an allowance for finance credit losses, which management believes is adequate for probable credit losses that can be reasonably estimated in its portfolio of finance receivable Contracts. Provision for loss is charged to the Company's Consolidated Statement of Operations. Net losses incurred on finance receivables are charged to the allowance. Management evaluates the adequacy of the allowance by examining current delinquencies, the characteristics of the portfolio, the value of the underlying collateral and historical loss trends. As conditions change, the Company's level of provisioning and/or allowance may change as well.

**Charge Off Policy**

Delinquent Contracts for which the related financed vehicle has been repossessed are generally charged off no later than the month in which the proceeds from the sale of the financed vehicle were received (see Repossessed and Other Assets below). The amount charged off is the remaining principal balance of the Contract, after the application of the net proceeds from the liquidation of the financed vehicle. With respect to delinquent Contracts for which the related financed vehicle has not been sold, the remaining principal balance thereof is generally charged off no later than the end of the month that the Contract becomes 120 days past due for CPS Program receivables and for non-CPS Program receivables, no later than the end of the month that the Contract becomes 180 days past due.

**Contract Acquisition Fees**

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

For Contracts purchased and securitized in pools which are structured as secured financings for financial accounting purposes, dealer acquisition fees reduce the carrying value of finance receivables and are accreted into earnings as an adjustment to the yield over the life of the loans using the interest method in accordance with Statement of Financial Accounting Standards No. 91, Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases .

F-11

---

**CONSUMER PORTFOLIO SERVICES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Effective January 1, 2005, the Company adopted the Accounting Standards Executive Committee's Statement of Position 03-3, "Accounting for Certain Loans or Debt Securities Acquired in a Transfer" (SOP 03-3), for loans acquired subsequent to December 31, 2004. Under SOP 03-3, dealer acquisition fees on loans purchased by the Company are not considered credit-related because there is no deterioration in credit quality between the time the loan originated and when it is acquired. The adoption of SOP 03-3 had no impact on the financial statements of the Company.

**Repossessed and Other Assets**

If a customer fails to make or keep promises for payments, or if the customer is uncooperative or attempts to evade contact or hide the vehicle, a supervisor will review the collection activity relating to the account to determine if repossession of the vehicle is warranted. Generally, such a decision will occur between the 45th and 90th day past the customer's payment due date, but could occur sooner or later, depending on the specific circumstances. At the time the vehicle is repossessed the Company will stop accruing interest in this Contract, and reclassify the remaining Contract balance to other assets. In addition the Company will apply a specific reserve to this Contract so that the net balance represents the estimated fair value less costs to sell. Included in other assets in the accompanying balance sheets are repossessed vehicles pending sale, net of the reserve, of \$4.2 million and \$2.7 million at December 31, 2005 and 2004, respectively.

Included in Other Assets are non-finance receivable assets totaling \$2.4 million as of December 31, 2005, net of a valuation allowance of \$1.9 million. The valuation allowance was established in 2005 and is included in general and administrative expenses in the Company's Consolidated Statement of Operations (See Note 13). Included in the \$1.9 million valuation allowance, is \$900,000 associated with related party receivables.

**Treatment of Securitizations**

Prior to July 2003, the disposition of Contracts in securitization transactions were structured as sales for financial accounting purposes, therefore, gain on sale was recognized on those securitization transactions in which the Company, or a wholly-owned, consolidated subsidiary of the Company, retained a residual interest in the Contracts that were sold to a wholly-owned, unconsolidated special purpose subsidiary. These securitization transactions include term securitizations (the purchaser holds the Contracts for substantially their entire term) and continuous or warehouse securitizations (which finance the acquisition of the Contracts for future sale into term securitizations).

The line item "Residual interest in securitizations" on the Company's Consolidated Balance Sheet represents the residual interests in term securitizations completed prior to July 2003. This line represents the discounted sum of expected future cash flows from these securitization trusts. Accordingly, the valuation of the residual is heavily dependent on estimates of future performance of the Contracts included in the term securitizations.

All subsequent securitizations were structured as secured financings. The warehouse securitizations are accordingly reflected in the line items "Finance receivables" and "Warehouse lines of credit" on the Company's Consolidated Balance Sheet, and the term securitizations are reflected in the line items "Finance receivables" and "Securitization trust debt."

The Company's securitization structure has generally been as follows:

The Company sells Contracts it acquires to a wholly-owned Special Purpose Subsidiary (SPS), which has been established for the limited purpose of buying and reselling the Company's Contracts. The SPS then transfers the same Contracts to another entity, typically a statutory trust (Trust). The Trust issues interest-bearing asset-backed securities (Notes), in a principal amount equal to or less than the aggregate principal balance of the Contracts. The Company

typically sells these Contracts to the Trust at face value and without recourse, except that representations and warranties similar to those provided by the Dealer to the Company are provided by the Company to the Trust. One or more investors purchase the Notes issued by the Trust (the Noteholders ); the proceeds from

F-12

---

**CONSUMER PORTFOLIO SERVICES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

the sale of the Notes are then used to purchase the Contracts from the Company. The Company may retain or sell subordinated Notes issued by the Trust or a related entity. The Company purchases a financial guaranty insurance policy, guaranteeing timely payment of principal and interest on the senior Notes, from an insurance company (a Note Insurer). In addition, the Company provides Credit Enhancement for the benefit of the Note Insurer and the Noteholders in three forms: (1) an initial cash deposit to a bank account (a Spread Account) held by the Trust, (2) overcollateralization of the Notes, where the principal balance of the Notes issued is less than the principal balance of the Contracts, and (3) in the form of subordinated Notes. The agreements governing the securitization transactions (collectively referred to as the Securitization Agreements) require that the initial level of Credit Enhancement be supplemented by a portion of collections from the Contracts until the level of Credit Enhancement reaches specified levels which are then maintained. The specified levels are generally computed as a percentage of the principal amount remaining unpaid under the related Contracts. The specified levels at which the Credit Enhancement is to be maintained will vary depending on the performance of the portfolios of Contracts held by the Trusts and on other conditions, and may also be varied by agreement among the Company, the SPS, the Note Insurers and the trustee. Such levels have increased and decreased from time to time based on performance of the various portfolios, and have also varied by Securitization Agreement. The Securitization Agreements generally grant the Company the option to repurchase the sold Contracts from the Trust when the aggregate outstanding balance of the Contracts has amortized to a specified percentage of the initial aggregate balance.

Beginning in the third quarter of 2003, the Company began to structure its term securitization transactions so that they would be treated for financial accounting purposes as borrowings secured by receivables, rather than as sales of receivables.

These changes collectively represent a deferral of revenue and acceleration of expenses, and thus a more conservative approach to accounting for the Company's operations compared to the previous term securitization transactions which were accounted for as sales at the consummation of the transaction. The changes have resulted in the Company initially reporting lower earnings than it would have reported if it had continued structuring its securitizations to require recognition of gain on sale.

Securitizations prior to July 2003 that were treated as sales for financial accounting purposes differ from secured financings in that the Trust to which the SPS sold the Contracts met the definition of a qualified special purpose entity under Statement of Financial Accounting Standards No. 140 (SFAS 140). As a result, assets and liabilities of the Trust are not consolidated into the Company's Consolidated Balance Sheet.

The Company's warehouse securitization structures are similar to the above, except that (i) the SPS that purchases the Contracts pledges the Contracts to secure promissory notes which it issues, (ii) the promissory notes are in an aggregate principal amount of not more than 77.0% to 80.0% of the aggregate principal balance of the Contracts (that is, at least 20.0% overcollateralization), and (iii) no increase in the required amount of Credit Enhancement is contemplated unless certain portfolio performance tests are breached. Upon each sale of Contracts in a securitization structured as a secured financing, the Company retains on its Consolidated Balance Sheet the Contracts securitized as assets and records the Notes issued in the transaction as indebtedness of the Company.

Under the prior securitizations structured as sales for financial accounting purposes, the Company removed from its Consolidated Balance Sheet the Contracts sold and added to its Consolidated Balance Sheet (i) the cash received, if any, and (ii) the estimated fair value of the ownership interest that the Company retains in Contracts sold in the securitization. That retained or residual interest (the Residual) consists of (a) the cash held in the Spread Account, if any, (b) overcollateralization, if any, (c) subordinated Notes retained, if any, and (d) receivables from Trust, which include the net interest receivables (NIRs). NIRs represent the estimated discounted cash flows to be received from the

Trust in the future, net of principal and interest payable with respect to the Notes, and certain expenses. The excess of the cash received and the assets retained by the Company over the allocated carrying value of the Contracts sold, less transaction costs, equals the net gain on sale of Contracts recorded by the Company. Until the maturity of these transactions, the Company's Consolidated Balance Sheet will reflect securitization transactions structured both as sales and as secured financings.

F-13

---



**CONSUMER PORTFOLIO SERVICES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

With respect to securitizations structured as sales for financial accounting purposes, the Company allocates its basis in the Contracts between the Contracts sold and the Residuals retained based on the relative fair values of those portions on the date of the sale. The Company recognizes gains or losses attributable to the change in the estimated fair value of the Residuals. Gains in fair value are recognized in the income statement with losses being recorded as an impairment loss in the income statement. The Company is not aware of an active market for the purchase or sale of interests such as the Residuals; accordingly, the Company determines the estimated fair value of the Residuals by discounting the amount of anticipated cash flows that it estimates will be released to the Company in the future (the cash out method), using a discount rate that the Company believes is appropriate for the risks involved. The anticipated cash flows include collections from both current and charged off receivables. The Company has used an effective pre-tax discount rate of 14% per annum except for certain collections from charged off receivables related to the Company's securitizations in 2001 and later where the Company has used a discount rate of 25%.

The Company receives periodic base servicing fees for the servicing and collection of the Contracts. In addition, the Company is entitled to the cash flows from the Trusts that represent collections on the Contracts in excess of the amounts required to pay principal and interest on the Notes, the base servicing fees, and certain other fees (such as trustee and custodial fees). Required principal payments on the Notes are generally defined as the payments sufficient to keep the principal balance of the Notes equal to the aggregate principal balance of the related Contracts (excluding those Contracts that have been charged off), or a pre-determined percentage of such balance. Where that percentage is less than 100%, the related Securitization Agreements require accelerated payment of principal until the principal balance of the Notes is reduced to the specified percentage. Such accelerated principal payment is said to create overcollateralization of the Notes.

If the amount of cash required for payment of fees, interest and principal exceeds the amount collected during the collection period, the shortfall is withdrawn from the Spread Account, if any. If the cash collected during the period exceeds the amount necessary for the above allocations, and there is no shortfall in the related Spread Account or other form of Credit Enhancement, the excess is released to the Company, or in certain cases is transferred to other Spread Accounts related to transactions insured by the same Note Insurer that may be below their required levels. If the total Credit Enhancement amount is not at the required level, then the excess cash collected is retained in the Trust until the specified level is achieved. Although Spread Account balances are held by the Trusts on behalf of the Company's SPS as the owner of the Residuals (in the case of securitization transactions structured as sales for financial accounting purposes) or the Trusts (in the case of securitization transactions structured as secured financings for financial accounting purposes), the cash in the Spread Accounts is restricted from use by the Company. Cash held in the various Spread Accounts is invested in high quality, liquid investment securities, as specified in the Securitization Agreements. In determining the value of the Residuals, the Company must estimate the future rates of prepayments, delinquencies, defaults, default loss severity, and recovery rates, as all of these factors affect the amount and timing of the estimated cash flows. The Company's estimates are based on historical performance of comparable Contracts.

Following a securitization that is structured as a sale for financial accounting purposes, interest income is recognized on the balance of the Residuals. In addition, the Company will recognize as a gain additional revenue from the Residuals if the actual performance of the Contracts is better than the Company's estimate of the value of the residual. If the actual performance of the Contracts were worse than the Company's estimate, then a downward adjustment to the carrying value of the Residuals and a related impairment charge would be required. In a securitization structured as a secured financing for financial accounting purposes, interest income is recognized when accrued under the terms of the related Contracts and, therefore, presents less potential for fluctuations in performance when compared to the approach used in a transaction structured as a sale for financial accounting purposes.

In all the Company's term securitizations, whether treated as secured financings or as sales, the Company has transferred the receivables (through a subsidiary) to the securitization Trust. The difference between the two structures is that in securitizations that are treated as secured financings the Company reports the assets and liabilities of the securitization Trust on its Consolidated Balance Sheet. Under both structures the Noteholders and the related securitization Trusts recourse to the Company for failure of the Contract obligors to make payments on a timely basis is limited to the Company's Finance receivables, Spread Accounts and Residuals.

F-14

---

**CONSUMER PORTFOLIO SERVICES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Servicing**

The Company considers the contractual servicing fee received on its managed portfolio held by non-consolidated subsidiaries to approximate adequate compensation. As a result, no servicing asset or liability has been recognized. Servicing fees received on its managed portfolio held by non-consolidated subsidiaries are reported as income when earned. Servicing fees received on its managed portfolio held by consolidated subsidiaries are included in interest income when earned. Servicing costs are charged to expense as incurred. Servicing fees receivable, which are included in Other Assets in the accompanying balance sheets, represent fees earned but not yet remitted to the Company by the trustee.

**Furniture and Equipment**

Furniture and equipment are stated at cost net of accumulated depreciation. The Company calculates depreciation using the straight-line method over the estimated useful lives of the assets, which range from three to five years. Assets held under capital leases and leasehold improvements are amortized over the lesser of the estimated useful lives of the assets or the related lease terms. Amortization expense on assets acquired under capital lease is included with depreciation expense on Company owned assets.

**Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed Of**

The Company accounts for long-lived assets in accordance with the provisions of SFAS No. 144, Accounting for the Impairment of Long-Lived Assets. This Statement requires that long-lived assets and certain identifiable intangibles be reviewed for impairment whenever events or changes in circumstances indicate that 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 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 amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of carrying amount or fair value less costs to sell.

**Other Income**

Other Income consists primarily of recoveries on previously charged off MFN Contracts, fees paid to the Company by Dealers for certain direct mail services the Company provides, refunds of sales taxes paid by obligors under the Contracts, and, in 2005 \$2.7 million in proceeds from sales of previously charged off Contracts to independent third parties. The recoveries on previously charged off MFN Contracts relate to Contracts that were acquired in the MFN acquisition. These recoveries totaled \$4.9 million, \$8.0 million and \$12.2 million for the years ended December 31, 2005, 2004 and 2003, respectively.

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****Earnings Per Share**

The following table illustrates the computation of basic and diluted earnings (loss) per share:

(in thousands, except per share data)	<b>2005</b>	<b>2004</b>	<b>2003</b>
Numerator:			
Numerator for basic and diluted earnings (loss) per share	\$ 3,372	\$ (15,888 )	\$ 395
Denominator:			
Denominator for basic earnings (loss) per share weighted average number of common shares outstanding during the year	21,627	21,111	20,263
Incremental common shares attributable to exercise of outstanding options and warrants	1,886		1,315
Denominator for diluted earnings (loss) per share	\$ 23,513	\$ 21,111	\$ 21,578
Basic earnings (loss) per share	\$ 0.16	\$ (0.75 )	\$ 0.02
Diluted earnings (loss) per share	\$ 0.14	\$ (0.75 )	\$ 0.02

Incremental shares of 1.1 million related to the conversion of subordinated debt have been excluded from the calculation for the year ended December 31, 2003 because the impact of assumed conversion of such subordinated debt is anti-dilutive. Incremental shares of 1.8 million shares related to stock options have been excluded from the diluted earnings (loss) per share calculation for the year ended December 31, 2004 because the impact is anti-dilutive.

In addition, options to purchase 639,000, 305,000 and 908,000 shares of common stock for the years ended December 31, 2005, 2004 and 2003, respectively, were excluded from the calculation of diluted earnings (loss) per share because the option exercise price was greater than the average market price of the shares.

**Deferral and Amortization of Debt Issuance Costs**

Costs related to the issuance of debt are amortized using the interest method over the contractual or expected term of the related debt.

**Income Taxes**

The Company and its subsidiaries file a consolidated federal income tax return and combined or stand-alone state franchise tax returns for certain states. The Company utilizes the asset and liability method of accounting for income taxes, under which deferred income taxes are recognized for the future tax consequences attributable to the differences between the financial statement values of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date. The Company has estimated a valuation allowance against that portion of the deferred tax asset whose utilization in future periods is not more than likely.

**Purchases of Company Stock**

The Company records purchases of its own common stock at cost.

F-16

---

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****Stock Option Plan**

As permitted by Statement of Financial Accounting Standards No. 123, Accounting for Stock-Based Compensation ( SFAS No. 123 ), the Company accounts for stock-based employee compensation plans in accordance with Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees and related interpretations, whereby stock options are recorded at intrinsic value equal to the excess of the share price over the exercise price at the date of grant. The Company provides the pro forma net income (loss), pro forma earnings (loss) per share, and stock based compensation plan disclosure requirements set forth in SFAS No. 123. The Company accounts for repriced options as variable awards.

In December 2005, the Compensation Committee of the Board of Directors approved accelerated vesting of all the outstanding stock options issued by the Company. Options to purchase 2,113,998 shares of the Company's common stock, which would otherwise have vested from time to time through 2010, became immediately exercisable as a result of the acceleration of vesting. The decision to accelerate the vesting of the options was made primarily to reduce non-cash compensation expenses that would have been recorded in the Company's income statement in future periods upon the adoption of Financial Accounting Standards Board Statement No. 123R in January 2006. The Company estimates that approximately \$3.5 million of future non-cash compensation expense will be eliminated as a result of the acceleration of vesting.

At the time of the acceleration of vesting, the Company accounted for its stock options in accordance with Accounting Principals Board Opinion No. 25, Accounting for Stock Issued to Employees. Consequently, the acceleration of vesting resulted in non-cash compensation charge of \$427,000 for the year ended December 31, 2005.

The per share weighted-average fair value of stock options granted during the years ended December 31, 2005, 2004 and 2003, was \$3.07, \$2.30, and \$2.09, respectively, at the date of grant. That fair value was computed using the Black-Scholes option-pricing model with the following weighted average assumptions:

	<b>Year Ended December 31,</b>		
	<b>2005</b>	<b>2004</b>	<b>2003</b>
Expected life (years)	6.50	6.50	7.63
Risk-free interest rate	4.32 %	4.48 %	4.16 %
Volatility	56.90 %	54.65 %	100.82 %
Expected dividend yield			

Compensation cost has been recognized for certain stock options in the Consolidated Financial Statements in accordance with APB Opinion No. 25. Had the Company determined compensation cost based on the fair value at the grant date for its stock options under Statement of Financial Accounting Standards No. 123 ( SFAS 123 ), Accounting for Stock Based Compensation, the Company's net income (loss) and earnings (loss) per share would have been adjusted to the pro forma amounts indicated below.

(in thousands, except per share data)	<b>Year Ended December 31,</b>		
	<b>2005</b>	<b>2004</b>	<b>2003</b>
Net income (loss)			
As reported	\$ 3,372	\$ (15,888 )	\$ 395

Edgar Filing: CONSUMER PORTFOLIO SERVICES INC - Form S-3/A

Pro forma		(648 )		(16,808 )		175
Earnings (loss) per share basic						
As reported	\$	0.16	\$	(0.75 )	\$	0.02
Pro forma		(0.03 )		(0.80 )		0.01
Earnings (loss) per share diluted						
As reported	\$	0.14	\$	(0.75 )	\$	0.02
Pro forma		(0.03 )		(0.80 )		0.01

F-17

**CONSUMER PORTFOLIO SERVICES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Segment Reporting**

Operations are managed and financial performance is evaluated on a Company-wide basis by a chief decision maker. Management has determined that the aggregation criteria of FASB Statement No. 131 have been met and accordingly, all of the Company's operations are aggregated in one reportable segment.

**New Accounting Pronouncements**

In December 2004, the Financial Accounting Standards Board ( FASB ) issued FASB Statement No. 123(R) (As Amended), Share-Based Payment ( FAS 123(R) or the Statement ). FAS 123 (R) and related interpretations require that the compensation cost relating to share-based payment transactions, including grants of employee stock options, be recognized in financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued. FAS 123(R) permits entities to use any option-pricing model that meets the fair value objective in the Statement. Modifications of share-based payments will be treated as replacement awards with the cost of the incremental value recorded in the financial statements.

The Statement is effective at the beginning of 2006 and will therefore be effective for the Company's first quarter of 2006. As of the effective date, the Company will apply the Statement using a modified version of prospective application. Under that transition method, compensation cost is recognized for (1) all awards granted after the required effective date and to awards modified, cancelled, or repurchased after that date and (2) the portion of prior awards for which the requisite service has not yet been rendered, based on the grant-date fair value of those awards calculated for pro forma disclosures under SFAS 123. As a result of the acceleration of vesting on all options outstanding in December 2005 there will be no effect on the Company's adoption of the statement in 2006 relating to such options currently outstanding.

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

**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 as of the date of the financial statements, as well as the reported amounts of income and expenses during the reported periods. Specifically, a number of estimates were made in connection with determining an appropriate allowance for finance credit losses, valuing the Residuals, computing the related gain on sale on the transactions that created the Residuals, and the recording of the deferred tax asset valuation allowance. These are material estimates that could be susceptible to changes in the near term and accordingly, actual results could differ from those estimates.



F-18

---

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****(2) Restricted Cash**

Restricted cash comprised the following components:

(in thousands)	<b>December 31,</b>	
	<b>2005</b>	<b>2004</b>
Securitization trust accounts	\$ 157,492	\$ 118,944
Litigation reserve	\$	5,503
Note purchase facility reserve	\$ 20	516
Other	\$ 150	150
Total restricted cash	\$ 157,662	\$ 125,113

Certain of the Company's operating agreements require that the Company establish cash reserves for the benefit of the other parties to the agreements, in case those parties are subject to any claims or exposure. In addition, certain of these agreements require that the Company establish amounts in reserve related to outstanding litigation.

**(3) Finance Receivables**

The following table presents the components of Finance Receivables, net of unearned interest:

(in thousands)	<b>December 31,</b>	
	<b>2005</b>	<b>2004</b>
Finance Receivables		
Automobile		
Simple Interest	\$ 933,510	\$ 522,346
Pre-compute, net of unearned interest	54,693	86,932
Finance Receivables, net of unearned interest	988,203	609,278
Less: Unearned acquisition fees and discounts	(16,899 )	(16,472 )
Finance Receivables	\$ 971,304	\$ 592,806

Finance receivables totaling \$5.1 million and \$5.4 million at December 31, 2005 and 2004, respectively, have been placed on non-accrual status as a result of their delinquency status.

The following table presents a summary of the activity for the allowance for credit losses, for the years ended December 31, 2005 and 2004:

(in thousands)	<b>December 31,</b>		
	<b>2005</b>	<b>2004</b>	<b>2003</b>
Balance at beginning of year	\$ 42,615	\$ 35,889	\$ 25,828
Addition to allowance for credit losses from acquisitions			24,271
Provision for credit losses	58,987	32,574	11,667

Edgar Filing: CONSUMER PORTFOLIO SERVICES INC - Form S-3/A

Charge-offs	(55,978 )	(34,636 )	(32,117 )
Recoveries	12,104	8,788	6,240
Balance at end of year	\$ 57,728	\$ 42,615	\$ 35,889

F-19

---

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****(4) Residual Interest in Securitizations**

The following table presents the components of the residual interest in securitizations and shown at their discounted amounts:

(in thousands)	<b>December 31,</b>	
	<b>2005</b>	<b>2004</b>
Cash, commercial paper, United States government securities and other qualifying investments (Spread Accounts)	\$ 12,748	\$ 17,776
Receivables from Trusts (NIRs)	5,798	12,483
Overcollateralization	6,674	16,644
Investment in subordinated certificates		3,527
Residual interest in securitizations	\$ 25,220	\$ 50,430

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

(dollars in thousands)	<b>December 31,</b>		
	<b>2005</b>	<b>2004</b>	<b>2003</b>
Undiscounted estimated credit losses	\$ 5,724	\$ 23,588	\$ 47,935
Managed portfolio held by non-consolidated subsidiary	103,130	233,621	425,534
Undiscounted estimated credit losses as a percentage of managed portfolio held by non-consolidated subsidiary	5.55 %	10.10 %	11.30 %

The key economic assumptions used in measuring the residual interest in securitizations at the date of securitization in 2003 are as follows: prepayment speed of 21.7%, net credit losses of 12.5%, and a discount rate of 14%. There were no securitizations accounted for as sales for financial accounting purposes in 2004 and 2005.

The key economic assumptions used in measuring all residual interest in securitizations as of December 31, 2005 and 2004 are included in the table below. The pre-tax discount rate remained constant at 14%, except for certain cash flows from charged off receivables related to the Company's securitizations from 2001 to 2003 where the Company has used a discount rate of 25%.

	<b>2005</b>	<b>2004</b>
Prepayment speed (Cumulative)	22.2% - 35.8%	20.0% - 30.5%
Net credit losses (Cumulative)	11.9% - 20.2%	13.0% - 20.5%

Static pool losses are calculated by summing the actual and projected future credit losses and dividing them by the original balance of each pool of assets.

F-20

---

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Key economic assumptions and the sensitivity of the current fair value of residual cash flows to immediate 10% and 20% adverse changes in those assumptions are as follows:

		<b>December 31,</b>
		<b>2005</b>
(dollars in thousands)		
Carrying amount/fair value of residual interest in securitizations	\$	25,220
Weighted average life in years	.	2.24
Prepayment Speed Assumption (Cumulative)	.	22.2% - 35.8%
Estimated fair value assuming 10% adverse change	. \$	25,168
Estimated fair value assuming 20% adverse change	.	25,119
Expected Net Credit Losses (Cumulative)	.	11.9% - 20.2%
Estimated fair value assuming 10% adverse change	. \$	23,937
Estimated fair value assuming 20% adverse change	.	22,656
Residual Cash Flows Discount Rate (Annual)	.	14.0% - 25.0%
Estimated fair value assuming 10% adverse change	. \$	24,636
Estimated fair value assuming 20% adverse change	.	24,071

These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in fair value based on 10% and 20% percent variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, in this table, the effect of a variation in a particular assumption on the fair value of the retained interest is calculated without changing any other assumption; in reality, changes in one factor may result in changes in another (for example, increases in market rates may result in lower prepayments and increased credit losses), which could magnify or counteract the sensitivities.

The following table summarizes the cash flows received from (paid to) the Company's unconsolidated securitization Trusts:

	<b>For the Year Ended December 31,</b>		
(in thousands)	<b>2005</b>	<b>2004</b>	<b>2003</b>
Releases of cash from Spread Accounts	\$ 7,420	\$ 17,175	\$ 25,934
Servicing Fees received	4,490	13,631	17,039
Net deposits to increase Credit Enhancement		(2,106 )	(20,867 )
Initial funding of Credit Enhancement			(18,736 )
Purchase of delinquent or foreclosed assets	(22,682 )	(44,473 )	(45,747 )
Repurchase of trust assets	(9,658 )		

The following table presents the credit loss and delinquency performance for the serviced portfolio:

(in thousands)	<b>Total Principal Amount of Contracts</b>		<b>Principal Amount of Contracts 60 Days or More Past Due</b>		<b>Net Credit Losses (1) for the Year Ended</b>	
	<b>At December 31,</b>		<b>At December 31,</b>		<b>December 31,</b>	
	<b>2005</b>	<b>2004</b>	<b>2005</b>	<b>2004</b>	<b>2005</b>	<b>2004</b>
Contracts held by consolidated subsidiaries	\$ 1,000,597	\$ 619,794	\$ 25,864	\$ 17,379	\$ 36,511	\$ 26,418
Contracts held by non-consolidated subsidiaries	103,130	233,621	4,263	10,037	14,184	36,042
SeaWest Third Party Portfolio	18,018	53,463	1,663	5,065	7,386	18,018
Total managed portfolio	\$ 1,121,745	\$ 906,878	\$ 31,790	\$ 32,481	\$ 58,081	\$ 80,478

(1) Includes recoveries on previously charged off MFN Contracts included in other income.

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****(5) Furniture and Equipment**

The following table presents the components of furniture and equipment:

(in thousands)	<b>December 31,</b>	
	<b>2005</b>	<b>2004</b>
Furniture and fixtures	\$ 3,780	\$ 3,744
Computer equipment	4,815	4,700
Leasing assets	673	673
Leasehold improvements	666	651
Other fixed assets	17	17
	9,951	9,785
Less: accumulated depreciation and amortization	(8,872 )	(8,218 )
	\$ 1,079	\$ 1,567

Depreciation expense totaled \$654,000, \$660,000 and \$878,000 for the years ended December 31, 2005, 2004 and 2003, respectively.

**(6) Restructuring Accruals****MFN Merger**

In connection with the MFN Merger, the Company subsequently terminated the MFN origination activities and consolidated certain activities of MFN. In connection therewith, the Company recognized certain liabilities related to the costs to exit these activities and terminate the affected employees of MFN. These activities include service departments such as accounting, finance, human resources, information technology, administration, payroll and executive management. Of these liabilities recognized at the merger date in the amount of \$6.2 million, only the accrual related to facility closures remained outstanding as of December 31, 2005 and 2004 in the amounts of \$545,000 and \$1.2 million respectively.

**TFC Merger**

In connection with the TFC Merger, the Company consolidated certain activities of CPS and TFC. As a result of this consolidation, the Company recognized certain liabilities related to the costs to integrate and terminate affected employees of TFC. These activities include service departments such as accounting, finance, human resources, information technology, administration, payroll and executive management. The total liabilities recognized by the Company at the time of the merger were \$4.5 million. These costs include the following:

(in thousands)	<b>December 31,</b>		<b>December 31,</b>		<b>December 31,</b>
	<b>2005(2)</b>	<b>Activity</b>	<b>2004</b>	<b>Activity</b>	<b>2003</b>
Severance Payments and consulting contracts (1)	\$ 109	\$ 309	\$ 418	\$ 1,908	\$ 2,326
Facilities closures	345	477	822	409	1,231



Other obligations					234		234
Total liabilities assumed	\$	454	\$	786	\$	1,240	\$ 2,551
							\$ 3,791

(1) For the period from December 31, 2003 to December 31, 2004 the activity resulting in a change of \$1.9 million, includes charges against the liability of \$621,000 and the reversal of \$1.3 million of costs that the Company no longer expects to incur. The \$1.3 was recorded in the statement of income as a reduction of operating expenses during the year ended December 31, 2004.

(2) The Company believes that this amount provides adequately for anticipated remaining costs related to exiting certain activities of TFC, and that amounts indicated above are reasonably allocated.

## CONSUMER PORTFOLIO SERVICES, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## (7) Securitization Trust Debt

The Company has completed a number of securitization transactions that are structured as secured borrowings for financial accounting purposes. The debt issued in these transactions is shown on the Company's consolidated balance sheets as Securitization trust debt, and the components of such debt are summarized in the following table:

Series	Final Scheduled Payment Date (1)	Receivables Pledged at December 31, 2005	Initial Principal	Outstanding Principal at December 31, 2005	Outstanding Principal at December 31, 2004	Weighted Average Interest Rate at December 31, 2005
MFN 2001-A	June 2007	\$	\$ 301,000	\$	\$ 3,382	
TFC 2002-1	August 2007		64,552		2,574	
TFC 2002-2	March 2008		62,589		9,152	
TFC 2003-1	January 2009	7,779	52,365	6,557	17,703	2.69%
CPS 2003-C	March 2010	32,063	87,500	30,550	53,456	3.57%
CPS 2003-D	October 2010	31,203	75,000	29,688	50,722	3.50%
CPS 2004-A	October 2010	40,316	82,094	40,225	66,737	3.62%
PCR 2004-1	March 2010	28,068	76,257	22,873	52,633	3.52%
CPS 2004-B	February 2011	53,330	96,369	52,704	84,185	4.17%
CPS 2004-C	April 2011	62,360	100,000	61,779	93,071	3.86%
CPS 2004-D	December 2011	84,034	120,000	82,801	109,200	4.44%
CPS 2005-A	October 2011	109,749	137,500	110,021	N/A	4.93%
CPS 2005-B	February 2012	121,440	130,625	113,194	N/A	4.16%
CPS 2005-C	May 2012	186,021	183,300	173,509	N/A	4.61%
CPS 2005-TFC	July 2012	78,991	72,525	72,525	N/A	5.72%
CPS 2005-D (2)	July 2012	86,083	127,600	127,600	N/A	4.98%
		\$ 921,437	\$ 1,769,276	\$ 924,026	\$ 542,815	

The Final Scheduled Payment Date represents final legal maturity of the securitization trust debt. Securitization trust debt is expected to become due and to be paid prior to those dates, based on amortization of the finance receivables pledged to the Trusts. Expected payments, which will depend on the performance of such receivables, as to which there can be no assurance, are \$328.7 million in 2006, \$223.7 million in 2007, \$160.5 million in 2008, \$114.6 million in 2009, \$75.1 million in 2010, and \$21.4 million in 2011.

Receivables Pledged at December 31, 2005 excludes approximately \$58.0 million in Contracts delivered to the Trust in January 2006 pursuant to a pre-funding structure.

All of the securitization trust debt was issued in private placement transactions to qualified institutional investors. The debt was issued through wholly-owned, bankruptcy remote subsidiaries of CPS, TFC or MFN, and is secured by the assets of such subsidiaries, but not by other assets of the Company. Principal and interest payments are guaranteed by

financial guaranty insurance policies.

The terms of the various Securitization Agreements related to the issuance of the securitization trust debt require that certain delinquency and credit loss criteria be met with respect to the collateral pool, and require that the Company maintain minimum levels of liquidity and net worth and not exceed maximum leverage levels and maximum financial losses. As a result of waivers and amendments to these covenants throughout 2004 and 2005, the Company was in compliance with all such covenants as of December 31, 2005. Without the waivers and amendments obtained in the first quarter of 2005, the Company would have been in breach of covenants related to maintaining a minimum level of net worth and incurring a maximum financial loss as of December 31, 2004.

The Company is responsible for the administration and collection of the Contracts. The Securitization Agreements also require certain funds be held in restricted cash accounts to provide additional collateral for the borrowings or to be applied to make payments on the securitization trust debt. As of December 31, 2005, restricted cash under the various agreements totaled approximately \$157.5 million. Interest expense on the securitization trust debt is composed of the stated rate of interest plus amortization of additional costs of borrowing. Additional costs of borrowing include facility fees, insurance and amortization of deferred financing costs. Deferred financing costs

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

related to the securitization trust debt are amortized in proportion to the principal distributed to the noteholders. Accordingly, the effective cost of borrowing of the securitization trust debt is greater than the stated rate of interest.

The wholly-owned, bankruptcy remote subsidiaries of CPS, MFN and TFC were formed to facilitate the above asset-backed financing transactions. Similar bankruptcy remote subsidiaries issue the debt outstanding under the Company's warehouse lines of credit. Bankruptcy remote refers to a legal structure in which it is expected that the applicable entity would not be included in any bankruptcy filing by its parent or affiliates. All of the assets of these subsidiaries have been pledged as collateral for the related debt. All such transactions, treated as secured financings for accounting and tax purposes, are treated as sales for all other purposes, including legal and bankruptcy purposes. None of the assets of these subsidiaries are available to pay other creditors of the Company or its affiliates.

**(8) Debt**

The terms of the Company's significant debt outstanding at December 31, 2005 and 2004 are summarized below:

(in thousands)	<b>December 31,</b>	
	<b>2005</b>	<b>2004</b>
<b>Residual interest financing</b>		
Notes secured by the Company's residual interests in its securitizations. The notes outstanding at December 31, 2004 were secured by eight securitization transactions and bore interest at 10.0% per annum. The notes outstanding at December 31, 2005 are secured by ten securitizations and bear interest at a blended interest rate of 8.36% per annum. In each period, the securitizations pledged include both sale transactions and secured financing transactions. The notes are non-recourse obligations of the Company with interest and principal to be paid solely from the cash distributions on the retained interests securing the notes. The notes outstanding at December 31, 2004 were issued in March 2004 with issuance costs of \$1.3 million and were repaid in full in August 2005. The notes outstanding at December 31, 2005 were issued in November 2005 with issuance costs of \$915,000 and have a final maturity of July 2011.	\$ 43,745	\$ 22,204
<b>Senior secured debt, related party</b>		
Notes payable to Levine Leichtman Capital Partners II, L.P. (LLCP). The notes consists of separate term notes that each bear interest at 11.75% per annum, require monthly interest payments and are due on various dates through December 2006, after having been amended from higher rates and earlier maturities. The Company incurred issuance and amendment fees aggregating \$1.3 million in relation to these notes. The notes are secured by all assets of the Company that are not pledged to securitization debt, and are the last in a series of borrowings from LLCP that have taken place since November 1998, which have also included the issuances to LLCP of warrants to purchase the Company's common stock. As of December 31, 2005 and 2004, a warrant to purchase 1,000 shares of common stock at \$0.01 per share remained outstanding which expire in April 2009.	\$ 40,000	\$ 59,829
<b>Subordinated debt</b>		
Notes bearing interest at 12.50% per annum and 12.00% per annum at December 31, 2005 and 2004 respectively. The Company incurred issuance costs of \$1.1 million	\$ 14,000	\$ 15,000

when the notes were issued in December 1995. The \$14.0 million outstanding was repaid on its maturity date in January 2006.

Renewable subordinated notes

Notes bearing interest ranging from 5.60% to 11.15%, with a weighted average rate of 8.53%, and with maturities from January 2006 to November 2015 with a weighted maturity of January 2008. The Company began issuing the notes in June 2005 and incurred issuance costs of \$250,000. Payments may be required monthly, quarterly, annually or upon maturity based on the terms of the individual notes.

\$	4,655	\$	
\$	102,400	\$	97,033

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

The costs incurred in conjunction with the above debt are recorded as deferred financing costs on the accompanying balance sheets and is more fully described in Note 1.

The Company must comply with certain affirmative and negative covenants related to debt facilities, which require, among other things, that the Company maintain certain financial ratios related to liquidity, net worth and capitalization. Further covenants include matters relating to investments, acquisitions, restricted payments and certain dividend restrictions.

The following table summarizes the contractual maturity amounts of debt as of December 31, 2005:

<b>Contractual maturity date</b>	<b>Residual interest financing (1)</b>	<b>Senior secured debt</b>	<b>Subordinated debt</b>	<b>Renewable subordinated notes</b>	<b>Total</b>
2006	\$ 17,986	\$ 40,000	\$ 14,000	\$ 1,643	\$ 73,629
2007	14,435			909	15,344
2008	7,644			1,562	9,206
2009	3,680			171	3,851
2010				279	279
Thereafter				91	91
	\$ 43,745	\$ 40,000	\$ 14,000	\$ 4,655	\$ 102,400

(1) The Contractual maturity date for the Residual interest financing is July 2011. The notes are expected to be paid prior to that date, based on the amortization of the related securitizations. Since the amortization of the related securitizations is based on the performance of the underlying finance receivables, there can be no assurance as to the exact timing of payments.

**(9) Shareholders Equity****Common stock**

Holders of common stock are entitled to such dividends as the Company's Board of Directors, in its discretion, may declare out of funds available, subject to the terms of any outstanding shares of preferred stock and other restrictions. In the event of liquidation of the Company, holders of common stock are entitled to receive, pro rata, all of the assets of the Company available for distribution, after payment of any liquidation preference to the holders of outstanding shares of preferred stock. Holders of the shares of common stock have no conversion or preemptive or other subscription rights and there are no redemption or sinking fund provisions applicable to the common stock.

The Company is required to comply with various operating and financial covenants defined in the agreements governing the warehouse lines of credit, senior debt, and subordinated debt. The covenants restrict the payment of certain distributions, including dividends (See Note 8.).

Included in common stock at December 31, 2003, is additional paid in capital of \$1.6 million related to the valuation of certain stock options as required by Financial Interpretation No. 44 ( FIN 44 ) or the valuation of conditionally granted options as required under Accounting Principals Board Opinion No. 25 ( APB 25 ). Included in compensation expense for the years ended December 31, 2005, 2004 and 2003, is \$644,000, \$271,000 and \$1.1 million related to the amortization of deferred compensation expense and valuation of stock options.

### **Stock Purchases**

During 2000, the Company's Board of Directors authorized the Company to purchase up to \$5 million of Company securities. In October 2002, the Board of Directors authorized the purchase of an additional \$5 million of outstanding debt or equity securities. In October 2004, the Board of Directors authorized the purchase of an additional \$5.0 million of outstanding debt or equity securities. As of December 31, 2005, the Company had purchased \$5.0 million in principal amount of the debt securities, and \$5.0 million of its common stock, representing 2,365,695 shares.

**CONSUMER PORTFOLIO SERVICES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Options and Warrants**

In 1991, the Company adopted and its sole shareholder approved the 1991 Stock Option Plan (the 1991 Plan ) pursuant to which the Company's Board of Directors may grant stock options to officers and key employees. The Plan, as amended, authorizes grants of options to purchase up to 2,700,000 shares of authorized but unissued common stock. Stock options are granted with an exercise price equal to the stock's fair market value at the date of grant. Stock options have terms that range from 7 to 10 years and vest over a range of 0 to 7 years. In addition to the 1991 Plan, in fiscal 1995, the Company granted 60,000 options to certain directors of the Company that vest over three years and expire nine years from the grant date. The Plan terminated in December 2001, without affecting the validity of the outstanding options.

In July 1997, the Company adopted and its shareholders approved the 1997 Long-Term Incentive Plan (the 1997 Plan ) pursuant to which the Company's Board of Directors may grant stock options, restricted stock and stock appreciation rights to employees, directors or employees of entities in which the Company has a controlling or significant equity interest. Options that have been granted under the 1997 Plan have been granted at an exercise price equal to (or greater than) the stock's fair market value at the date of the grant, with terms of 10 years and vesting generally over 5 years. In 2001, the shareholders of the Company approved an amendment to the 1997 Plan providing that an aggregate maximum of 3,400,000 shares of the Company's common shares may be subject to awards under the 1997 Plan. In 2003, the shareholders of the Company approved an amendment to the 1997 Plan to further increase the aggregate maximum number of shares that may be granted within the Plan to 4,900,000 shares. A further increase to 6,900,000 shares in the aggregate maximum number of shares that may be granted was approved by the shareholders in 2004.

In October 1998, the Company's Board of Directors approved a plan to cancel and reissue certain stock options previously granted to key employees of the Company. All options granted prior to October 22, 1998, with an option price greater than \$3.25 per share, were repriced to \$3.25 per share. In conjunction with the repricing, a one-year period of non-exercisability was placed on all repriced options, which period ended on October 21, 1999.

In October 1999, the Company's Board of Directors approved a plan to cancel and reissue certain stock options previously granted to key employees of the Company. All options granted prior to October 29, 1999, with an option price greater than \$0.625 per share, were repriced to \$0.625 per share. In conjunction with the repricing, a six-month period of non-exercisability was placed on all repriced options, which period ended on April 29, 2000.

At December 31, 2005, there were a total of 165,261 additional shares available for grant under the 1997 Plan and the 1991 Plan. Of the options outstanding at December 31, 2005, 2004 and 2003, 4,863,654, 1,611,182, and 1,168,042, respectively, were then exercisable, with weighted-average exercise prices of \$3.38, \$2.25, and \$1.71, respectively.



**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Stock option activity during the periods indicated is as follows:

(in thousands, except per share data)	<b>Number of Shares</b>	<b>Weighted Average Exercise Price</b>
Balance at December 31, 2002	4,032	\$ 1.64
Granted	1,013	2.46
Exercised	609	0.93
Canceled	564	1.69
Balance at December 31, 2003	3,872	1.96
Granted	958	3.96
Exercised	575	1.23
Canceled	173	2.29
Balance at December 31, 2004	4,082	2.52
Granted	1,451	5.39
Exercised	415	2.08
Canceled	254	3.17
Balance at December 31, 2005	4,864	\$ 3.38

The per share weighted average fair value of stock options granted whose exercise price was equal to the market price of the stock on the grant date during the years ended December 31, 2005, 2004 and 2003, was \$2.77, \$2.30, and \$2.09, respectively.

The per share weighted average fair value and exercise price of stock options granted whose exercise price was above the market price of the stock on the grant date during the year ended December 31, 2005 was \$3.61 and \$6.00, respectively. The Company did not issue any stock options above the market price of the stock during the year ended December 31, 2004 and 2003.

The Company did not issue any stock options below the market price of the stock on the grant date.

During 2002, the Company's Board of Directors approved a program whereby officers of the Company would be loaned amounts sufficient to enable them to exercise certain of their outstanding options. See Note 13.

At December 31, 2005, the range of exercise prices, the number, weighted-average exercise price and weighted-average remaining term of options outstanding and the number and weighted-average price of options currently exercisable are as follows:

<b>Range of Exercise Prices (per share)</b>	<b>Options Outstanding</b>		<b>Weighted Average Exercise Price Per</b>	<b>Options Exercisable</b>	
	<b>Number Outstanding</b>	<b>Weighted Average Remaining Term</b>		<b>Number Exercisable</b>	<b>Weighted Average Exercise Price Per</b>

		<b>(Years)</b>	<b>Share</b>		<b>Share</b>
				(in thousands, except per share data)	
\$0.63 - \$1.50	858	6.43	\$ 1.47	858	\$ 1.47
\$1.51 - \$2.50	1,092	5.61	1.93	1,092	1.93
\$2.51 - \$4.00	1,225	8.00	3.46	1,225	3.46
\$4.01 - \$5.04	1,035	8.53	4.74	1,035	4.74
\$5.05 - \$6.10	654	9.90	5.99	654	5.99

F-27

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

On November 17, 1998, in conjunction with the issuance of a \$25.0 million subordinated promissory note to an affiliate of LLC, the Company issued warrants to purchase up to 3,450,000 shares of common stock at \$3.00 per share, exercisable through November 30, 2005. In April 1999, in conjunction with the issuance of \$5.0 million of an additional subordinated promissory note to an affiliate of LLC, the Company issued additional warrants to purchase 1,335,000 shares of the Company's common stock at \$0.01 per share to LLC. As part of the purchase agreement, the existing warrants to purchase 3,450,000 shares at \$3.00 per share were exchanged for warrants to purchase 3,115,000 shares at a price of \$0.01 per share. The aggregate value of the warrants, \$12.9 million, which is comprised of \$3.0 million from the original warrants issued in November 1998 and \$9.9 million from the repricing and additional warrants issued in April 1999, is reported as deferred interest expense to be amortized over the expected life of the related debt, five years. As of December 31, 2005 and 2004, 1,000 warrants remained unexercised which expire in April 2009. Such warrants, and the 4,449,000 shares of common stock have, upon the exercise of such warrants, not been registered for public sale. However, the holder has the right to require the Company register the warrants and common stock for public sale in the future.

Also in November 1998, the Company entered into an agreement with the Note Insurer of its asset-backed securities. The agreement committed the Note Insurer to provide insurance for the securitization of \$560.0 million in asset-backed securities, of which \$250.0 million remained at December 31, 1998. The agreement provides for a 3% initial Spread Account deposit. As consideration for the agreement, the Company issued warrants to purchase up to 2,525,114 shares of common stock at \$3.00 per share, subject to anti-dilution adjustments. The warrants were fully exercisable on the date of grant and expired in December 2003. In November 2003, the Company purchased the warrants from the Note Insurer for \$896,415.

The Company on August 4, 2005, issued six-year warrants with respect to 272,000 shares of its common stock, in a transaction exempted from the registration requirements of the Securities Act of 1933 as a transaction not involving a public offering. The warrants are exercisable at \$4.85 per share, and were issued to the lender's nominee in settlement of a claim against the Company that arose out of a loan of \$500,000 made in September 1998. The Company and the claimant dispute whether the loan was to the Company or to Stanwich Financial Services Corp. ( Stanwich ). The Company received in exchange for the warrants an assignment of the lender's claim in bankruptcy against Stanwich, as well as a release of all claims against the Company. The Company estimated the value of the warrants to be \$794,000 using a Black-Scholes model, assuming a risk-free interest rate of 3.41%, a six year life and stock price volatility of 63%. The Company included the value of the warrant, net of a previously recorded accrual of \$500,000, in general & administrative expense for the year ended December 31, 2005.

**(10) Net Gain on Sale of Contracts**

The following table presents the components of the net gain on sale of Contracts:

(in thousands)	<b>Year Ended December 31, 2003</b>
Gain recognized on sale of Contracts	\$ 8,433
Deferred acquisition fees and discounts	\$ 4,590

Expenses related to sales	\$	(2,076 )
Provision for credit losses	\$	(526 )
Net gain on sale of Contracts	\$	10,421

No gain on sale was recorded in the year ended December 31, 2005 and 2004 due to the decision in July 2003 to structure future securitizations as secured financings, rather than as sales.

F-28

---

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****(11) Interest Income**

The following table presents the components of interest income:

(in thousands)	Year Ended December 31,		
	2005	2004	2003
Interest on Finance Receivables	\$ 163,552	\$ 99,701	\$ 40,380
Residual interest income	\$ 5,338	4,634	16,178
Other interest income	\$ 2,944	1,483	1,606
Net interest income	\$ 171,834	\$ 105,818	\$ 58,164

As a result of the uncertainty of collection of the residual assets, the Company ceased accruing interest on the residual assets from May 2004 through December 2004. In January 2005, the Company resumed accretion of interest on the residual assets after it determined that there was no longer any significant uncertainty as to the collection of the assets.

**(12) Income Taxes**

Income taxes consist of the following:

(in thousands)	Year Ended December 31,		
	2005	2004	2003
Current:			
Federal	\$ 5,340	\$ 712	\$ 2,781
State	\$ 1,687	862	356
	7,027	1,574	3,137
Deferred:			
Federal	\$ (3,537 )	(5,859 )	(25,345 )
State	\$ (2,114 )	(2,282 )	(4,141 )
Change in valuation allowance	\$ (1,376 )	6,567	22,915
	(7,027 )	(1,574 )	(6,571 )
Income tax benefit	\$	\$	\$ (3,434 )

The Company's effective tax expense/(benefit) for the years ended December 31, 2005, 2004 and 2003, differs from the amount determined by applying the statutory federal rate of 35% to income (loss) before income taxes as follows:

(in thousands)	Year Ended December 31,		
	2005	2004	2003
Expense (benefit) at federal tax rate	\$ 1,180	\$ (5,561 )	\$ (1,064 )
State franchise tax, net of federal income tax benefit	\$ (277 )	(1,015 )	(2,460 )

Edgar Filing: CONSUMER PORTFOLIO SERVICES INC - Form S-3/A

Other	\$	473	9	92
Debt Forgiveness	\$			(22,917 )
Valuation allowance	\$	(1,376 )	6,567	22,915
	\$		\$	\$ (3,434 )

F-29

---

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

The tax affected cumulative temporary differences that give rise to deferred tax assets and liabilities as of December 31, 2005 and 2004 are as follows:

(in thousands)	<b>December 31,</b>	
	<b>2005</b>	<b>2004</b>
<b>Deferred Tax Assets:</b>		
Finance receivables	\$ 21,493	\$ 18,090
Provision for loan loss	961	
Accrued liabilities	3,141	5,751
Furniture and equipment	189	1,016
Equity investment		82
NOL carryforwards and BILs	24,137	27,702
Minimum tax credit		697
Pension Accrual	1,313	801
Other	1,830	831
Total deferred tax assets	53,064	54,970
Valuation allowance	(43,724 )	(45,100 )
	9,340	9,870
<b>Deferred Tax Liabilities:</b>		
NIRs	(1,808 )	(1,407 )
Provision for loan loss		(8,463 )
Total deferred tax liabilities	(1,808 )	(9,870 )
Net deferred tax asset	\$ 7,532	\$

As part of the MFN Merger, CPS acquired certain net operating losses and built-in loss assets. Moreover, MFN has undergone an ownership change for purposes of Internal Revenue Code ( IRC ) section 382. In general, IRC section 382 imposes an annual limitation on the ability of a loss corporation (i.e., a corporation with a net operating loss ( NOL ) carryforward, credit carryforward, or certain built-in losses ( BILs )) to utilize its pre-change NOL carryforwards or BILs to offset taxable income arising after an ownership change. During 1999, MFN recorded an extraordinary gain from the discharge of indebtedness related to the emergence from Bankruptcy. This gain was not taxable under IRC section 108. In accordance with the rules under IRC section 108, MFN has reduced certain tax attributes including unused net operating losses and tax basis in certain MFN assets. Deferred taxes have been provided for the estimated tax effect of the future reversing timing differences related to the discharge of indebtedness gain as reduced by the tax attributes. Additionally, the Company has established a valuation allowance of \$31.0 million against MFN's deferred tax assets, as it is not more than likely that these amounts will be realized in the future.

As part of the TFC Merger, CPS acquired certain built in loss assets. Moreover, TFC has undergone an ownership change for purposes of Internal Revenue Code ( IRC ) section 382. In general, IRC section 382 imposes an annual limitation on the ability of a loss corporation (i.e., a corporation with a net operating loss ( NOL ) carryforward, credit

carryforward, or certain built-in losses ( BILs )) to utilize its pre-change NOL carryforwards or BILs to offset taxable income arising after an ownership change. Additionally, the Company has established a valuation allowance of \$10.0 million against TFC s deferred tax assets, as it is not more than likely that these amounts will be realized in the future.

In determining the possible future realization of deferred tax assets, the Company considers the taxes paid in the current and prior years that may be available to recapture as well as future taxable income from the following sources: (a) reversal of taxable temporary differences, (b) future operations exclusive of reversing temporary differences, and (c) tax planning strategies that, if necessary, would be implemented to accelerate taxable income into years in which net operating losses might otherwise expire.

F-30

---



**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

As of December 31, 2005, the Company has net operating loss carryforwards for federal and state income tax purposes of \$10.2 million (all of which is subject to IRC 382 limitations) and \$4.2 million, respectively, which are available to offset future taxable income, if any, subject to IRC section 382 limitations, through 2021 and 2012-2013, respectively.

The statute of limitations on certain of the Company's tax returns are open and the returns could be audited by the various tax authorities. From time to time, there may be differences in opinions with respect to the tax treatment accorded to certain transactions. When, and if, such differences occur and become probable and estimable, such amounts will be recognized.

**(13) Related Party Transactions****CPS Leasing, Inc. Related Party Direct Lease Receivables**

Included in other assets in the Company's Consolidated Balance Sheet are direct lease receivables due to CPS Leasing, Inc. from related parties, primarily companies affiliated with the Company's former Chairman of the Board of Directors. Such related party direct lease receivables net of a valuation allowance totaled approximately \$552,000 and \$1.8 million at December 31, 2005 and 2004, respectively.

**Loans to Officers to Exercise Certain Stock Options**

During 2002, the Company's Board of Directors approved a program under which officers of the Company would be advanced amounts sufficient to enable them to exercise certain of their outstanding options. Such loans were available for a limited period of time, and available only to exercise previously repriced options. The loans bear interest at a rate of 5.50% per annum, and are due in 2007. At December 31, 2005 and 2004, there was \$434,000 and \$454,000, respectively outstanding related to these loans. Such amounts have been recorded as contra-equity within common stock in the Shareholders' Equity section of the Company's Consolidated Balance Sheet.

**(14) Commitments and Contingencies****Leases**

The Company leases its facilities and certain computer equipment under non-cancelable operating leases, which expire through 2010. Future minimum lease payments at December 31, 2005, under these leases are due during the years ended December 31 as follows:

(in thousands)	<b>Amount</b>
2006	\$ 4,353
2007	3,781
2008	2,407
2009	341
2010	203
Total minimum lease payments	\$ 11,085

Rent expense for the years ended December 31, 2005, 2004 and 2003, was \$3.4million, \$3.5 million, and \$3.9 million, respectively.

The Company's facility lease contains certain rental concessions and escalating rental payments, which are recognized as adjustments to rental expense and are amortized on a straight-line basis over the term of the lease.

F-31

---

**CONSUMER PORTFOLIO SERVICES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

During 2005, 2004 and 2003, the Company received \$482,000, \$385,000 and \$170,000, respectively, of sublease income, which is included in occupancy expense. Future minimum sublease payments totaled \$507,000 at December 31, 2005.

**Litigation**

*Stanwich Litigation.* CPS was for some time a defendant in a class action (the Stanwich Case ) brought in the California Superior Court, Los Angeles County. The original plaintiffs in that case were persons entitled to receive regular payments (the Settlement Payments ) under out-of-court settlements reached with third party defendants. Stanwich Financial Services Corp. ( Stanwich ), an affiliate of the former chairman of the board of directors of CPS, is the entity that was obligated to pay the Settlement Payments. Stanwich has defaulted on its payment obligations to the plaintiffs and in June 2001 filed for reorganization under the Bankruptcy Code, in the federal Bankruptcy Court of Connecticut. At December 31, 2004, CPS was a defendant only in a cross-claim brought by one of the other defendants in the case, Bankers Trust Company, which asserted a claim of contractual indemnity against CPS.

CPS subsequently settled the cross-claim of Bankers Trust by payment of \$3.24 million, on or about February 8, 2005. Pursuant to that settlement, the court has dismissed the cross-claim, with prejudice. The amount paid by the Company was accrued for and included in Accounts payable and accrued expenses in the Company s balance sheet as of December 31, 2004.

In November 2001, one of the defendants in the Stanwich Case, Jonathan Pardee, asserted claims for indemnity against the Company in a separate action, which is now pending in federal district court in Rhode Island. The Company has filed counterclaims in the Rhode Island federal court against Mr. Pardee, and has filed a separate action against Mr. Pardee s Rhode Island attorneys, in the same court. The action of Mr. Pardee against CPS is stayed, awaiting resolution of an adversary action brought against Mr. Pardee in the bankruptcy court, which is hearing the bankruptcy of Stanwich.

The reader should consider that any adverse judgment against CPS in the Stanwich Case (or the related case in Rhode Island) for indemnification, in an amount materially in excess of any liability already recorded in respect thereof, could have a material adverse effect on the Company s financial position.

*Other Litigation.* On June 2, 2004, Delmar Coleman filed a lawsuit in the circuit court of Tuscaloosa, Alabama, alleging that plaintiff Coleman was harmed by an alleged failure to refer, in the notice given after repossession of his vehicle, to the right to purchase the vehicle by tender of the full amount owed under the retail installment contract. Plaintiff seeks damages in an unspecified amount, on behalf of a purported nationwide class. CPS removed the case to federal bankruptcy court, and filed a motion for summary judgment as part of its adversary proceeding against the plaintiff in the bankruptcy court. The federal bankruptcy court granted the plaintiff s motion to send the matter back to Alabama state court. CPS has appealed the ruling. Although CPS believes that it has one or more defenses to each of the claims made in this lawsuit, no discovery has yet been conducted and the case is still in its earliest stages. Accordingly, there can be no assurance as to its outcome.

In June 2004, Plaintiff Jeremy Henry filed a lawsuit against the Company in the California Superior Court, San Diego County, alleging improper practices related to the notice given after repossession of a vehicle that he purchased. Plaintiff s motion for a certification of a class has been denied, and is the subject of an appeal now before the California Court of Appeal. Irrespective of the outcome of that appeal, as to which there can be no assurance, the Company has a number of defenses that may be asserted with respect to the claims of plaintiff Henry.

In August and September 2005, two plaintiffs represented by the same law firm filed substantially identical lawsuits in the federal district court for the northern district of Illinois, each of which purports to be a class action, and each of which alleges that CPS improperly accessed consumer credit information. CPS has reached agreements in principle to settle these cases, which await confirmation by the court.

F-32

---

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

The Company has recorded a liability as of December 31, 2005 that it believes represents a sufficient allowance for legal contingencies. Any adverse judgment against the Company, if in an amount materially in excess of the recorded liability, could have a material adverse effect on the financial position of the Company. The Company is involved in various legal matters arising in the normal course of business. Management believes that any liability as a result of those matters would not have a material effect on the Company's financial position, Results of Operations or Cash Flows.

**(15) Employee Benefits**

The Company sponsors a pretax savings and profit sharing plan (the 401(k) Plan) qualified under section 401(k) of the Internal Revenue Code. Under the 401(k) Plan, eligible employees are able to contribute up to 15% of their compensation (subject to stricter limitation in the case of highly compensated employees). The Company may, at its discretion, match 100% of employees' contributions up to \$1,000 per employee per calendar year. The Company's contributions to the 401(k) Plan were \$439,000 and \$409,000 for the year ended December 31, 2005 and 2004, respectively. The Company did not make a matching contribution in 2003.

The Company also sponsors the MFN Financial Corporation Pension Plan (the Plan). The Plan benefits were frozen June 30, 2001. The following table sets forth the plan's benefit obligations, fair value of plan assets, and funded status at December 31, 2005 and 2004:

(in thousands)	<b>December 31,</b>	
	<b>2005</b>	<b>2004</b>
<b>Change in Projected Benefit Obligation</b>		
Projected benefit obligation, beginning of year	\$ 13,683	\$ 15,023
Service cost		
Interest cost	845	821
Actuarial (gain) loss	1,867	(1,616)
Benefits paid	(596)	(545)
Projected benefit obligation, end of year	\$ 15,799	\$ 13,683

The accumulated benefit obligation for the plan was \$15.8 million and \$13.7 million at December 31, 2005 and 2004, respectively.

**Change in Plan Assets**

Fair value of plan assets, beginning of year	\$ 13,287	\$ 11,253
Return on assets	\$ 973	1,483
Employer contribution	\$ 207	1,149
Expenses	\$ (59)	(53)
Benefits paid	\$ (596)	(545)
Fair value of plan assets, end of year	\$ 13,812	\$ 13,287

(in thousands)	December 31,	
	2005	2004
<b>Reconciliation of funded status of the plan and net amount recognized</b>		
Funded status of the plan	\$ (1,987 )	\$ (396 )
Unrecognized loss	\$ 4,071	2,062
Unrecognized transition asset	\$ (11 )	(46 )
Unrecognized prior service cost	\$	
Net amount recognized	\$ 2,073	\$ 1,620

F-33

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Weighted average assumptions used to determine benefit obligations and cost at December 31, 2005 and 2004 were as follows:

**Weighted average assumptions used to determine benefit obligations**

Discount rate	5.50%	6.25%
Rate of compensation increase	N/A	N/A

**Weighted average assumptions used to determine net periodic benefit cost**

Discount rate	5.50%	6.25%
Expected return on plan assets	8.50%	9.00%
Rate of compensation increase	N/A	N/A

The Company's overall expected long-term rate of return on assets is 8.50% per annum as of December 31, 2005. The expected long-term rate of return is based on the weighted average of historical returns on individual asset categories, which are described in more detail below.

**Amounts recognized on Consolidated Balance Sheet**

Prepaid benefit cost	\$	\$
Accrued benefit liability	(1,987 )	(396 )
Intangible asset		
Accumulated other comprehensive loss, pretax	4,060	2,016
Net amount recognized	\$ 2,073	\$ 1,620

**Components of net periodic benefit cost**

Service cost	\$	\$
Interest Cost	845	821
Expected return on assets	(1,104 )	(1,041 )
Amortization of transition (asset)/obligation	(35 )	(35 )
Amortization of prior service cost		
Recognized net actuarial loss	48	69
Net periodic benefit cost	\$ (246 )	\$ (186 )

**Unfunded Accumulated Benefit Obligation at Year-End**

Projected Benefit Obligation	\$15,799	\$ 13,683
Accumulated Benefit Obligation	15,799	13,683
Fair Value of Plan Assets	13,812	13,288

F-34

---



**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

The weighted average asset allocation of the Company's pension benefits at December 31, 2005 and 2004 were as follows:

**Weighted Average Asset Allocation at Year-End****Asset Category**

Domestic equity funds	61.9%	60.9%
International equity funds	13.1%	11.9%
Domestic fixed income funds	25.0%	27.1%
Other	0.0%	0.1%
Total	100.0%	100.0%

**Cash Flows****Expected Benefit Payouts**

2006	\$ 476
2007	\$ 511
2008	\$ 570
2009	\$ 574
2010	\$ 593
Years 2011 - 2015	\$ 3,859
Anticipated Contributions in 2006	\$

The Company's investment policies and strategies for the pension benefits plan utilize a target allocation of 70% equity securities and 30% fixed income securities. The Company's investment goals are to maximize returns subject to specific risk management policies. The Company addresses risk management and diversification by the use of a professional investment advisor and several sub-advisors which invest in domestic and international equity securities and domestic fixed income securities. Each sub-advisor focuses its investments within a specific sector of the equity or fixed income market. For the sub-advisors focused on the equity markets, the sectors are differentiated by the market capitalization and the relative valuation of the underlying issuer. For the sub-advisors focused on the fixed income markets, the sectors are differentiated by the credit quality and the maturity of the underlying fixed income investment. The investments made by the sub-advisors are readily marketable and can be sold to fund benefit payment obligations as they become payable.

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****(16) Fair Value of Financial Instruments**

The following summary presents a description of the methodologies and assumptions used to estimate the fair value of the Company's financial instruments. Much of the information used to determine fair value is highly subjective. When applicable, readily available market information has been utilized. However, for a significant portion of the Company's financial instruments, active markets do not exist. Therefore, considerable judgments were required in estimating fair value for certain items. The subjective factors include, among other things, the estimated timing and amount of cash flows, risk characteristics, credit quality and interest rates, all of which are subject to change. Since the fair value is estimated as of December 31, 2005 and 2004, the amounts that will actually be realized or paid at settlement or maturity of the instruments could be significantly different. The estimated fair values of financial assets and liabilities at December 31, 2005 and 2004, were as follows:

(in thousands)	<b>December 31,</b>			
	<b>2005</b>		<b>2004</b>	
<b>Financial Instrument</b>	<b>Carrying Value</b>	<b>Fair Value</b>	<b>Carrying Value</b>	<b>Fair Value</b>
Cash and cash equivalents	\$ 17,789	\$ 17,789	\$ 14,366	\$ 14,366
Restricted cash and cash equivalents	157,662	157,662	125,113	125,113
Finance receivables, net	913,576	913,576	550,191	550,191
Residual interest in securitizations	25,220	25,220	50,430	50,430
Accrued interest receivable	10,930	10,930	6,411	6,411
Note receivable and accrued interest	2,178	2,178	2,800	2,800
Warehouse lines of credit	35,350	35,350	34,279	34,279
Notes payable	211	211	1,421	1,421
Residual interest financing	43,745	43,745	22,204	22,204
Securitization trust debt	924,026	914,901	542,815	539,749
Senior secured debt	40,000	40,000	59,829	59,829
Subordinated renewable notes	4,655	4,655		
Subordinated debt	14,000	14,000	15,000	15,113

**Cash, Cash Equivalents and Restricted Cash**

The carrying value equals fair value.

**Finance Receivables, net**

The carrying value approximates fair value because the related interest rates are estimated to reflect current market conditions for similar types of instruments.

**Residual Interest in Securitizations**

The fair value is estimated by discounting future cash flows using credit and discount rates that the Company believes reflect the estimated credit, interest rate and prepayment risks associated with similar types of instruments.

**Accrued Interest Receivable**

The carrying value approximates fair value because the related interest rates are estimated to reflect current market conditions for similar types of instruments.

**CONSUMER PORTFOLIO SERVICES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note Receivable**

The fair value is estimated by discounting future cash flows using credit and discount rates that the Company believes reflect the estimated credit and interest rate risks associated with similar types of instruments.

**Warehouse Lines of Credit, Notes Payable, Residual Interest Financing, and Senior Secured Debt and Subordinated Renewable Notes**

The carrying value approximates fair value because the related interest rates are estimated to reflect current market conditions for similar types of secured instruments.

**Securitization Trust Debt**

The fair value is estimated by discounting future cash flows using interest rates that the Company believes reflect the current market rates.

**Subordinated Debt**

The fair value is based on a market quote.

**(17) Liquidity**

The Company's business requires substantial cash to support its purchases of Contracts and other operating activities. The Company's primary sources of cash have been cash flows from operating activities, including proceeds from sales of Contracts, amounts borrowed under various revolving credit facilities (also sometimes known as warehouse credit facilities), servicing fees on portfolios of Contracts previously sold in securitization transactions or serviced for third parties, customer payments of principal and interest on finance receivables, fees for origination of Contracts, and releases of cash from securitized portfolios of Contracts in which the Company has retained a residual ownership interest and from the Spread Accounts associated with such pools. The Company's primary uses of cash have been the purchases of Contracts, repayment of amounts borrowed under lines of credit and otherwise, operating expenses such as employee, interest, occupancy expenses and other general and administrative expenses, the establishment of Spread Accounts and initial overcollateralization, if any, and the increase of Credit Enhancement to required levels in securitization transactions, and income taxes. There can be no assurance that internally generated cash will be sufficient to meet the Company's cash demands. The sufficiency of internally generated cash will depend on the performance of securitized pools (which determines the level of releases from those portfolios and their related Spread Accounts), the rate of expansion or contraction in the Company's managed portfolio, and the terms upon which the Company is able to acquire, sell, and borrow against Contracts.

Net cash provided by operating activities for the years ended December 31, 2005, 2004 and 2003 was \$36.7 million, \$9.9 million and \$98.9 million, respectively. Cash from operating activities is generally provided by the net releases from the Company's securitization Trusts. The increase in 2005 vs. 2004 is due in part to the Company's increased net earnings before the significant increase in the provision for credit losses. The decrease in 2004 vs. 2003 is primarily the result of the Company's decision, in July 2003, to treat all of its future securitizations as secured financings. As a result 2005 and 2004 includes no activity related to Contracts held for sale.

Net cash used in investing activities for the years ended December 31, 2005, 2004 and 2003, was \$411.7 million, \$314.0 million, and \$178.9 million, respectively. Cash used in investing activities has generally related to purchases of

Contracts, the cost of the SeaWest Asset Acquisition and the acquisition of TFC. Purchase of finance receivables held for investors were \$691.3, \$506.0 and \$175.3 in 2005, 2004 and 2003, respectively. Cash used in the TFC Merger, net of the cash acquired in the transaction, totaled \$10.2 million for the year ended December 31, 2003.

F-37

---

**CONSUMER PORTFOLIO SERVICES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Net cash provided by financing activities for the year ended December 31, 2005, was \$378.4 million compared with \$285.3 million in 2004 and \$80.3 million for the year ended December 31, 2003. Cash used or provided by financing activities is primarily attributable to the issuance or repayment of debt. In connection with the TFC Merger the Company assumed securitization trust debt related to three securitization transactions held by consolidated subsidiaries and assumed additional subordinated debt. With the change in the securitization structure implemented in the third quarter of 2003, \$662.4 million of securitization trust debt was issued in 2005 as compared to \$474.7 million in 2004 and \$154.4 million in 2003.

Contracts are purchased from Dealers for a cash price approximating their principal amount, adjusted for an acquisition fee which may either increase or decrease the Contract purchase price, and generate cash flow over a period of years. As a result, the Company has been dependent on warehouse credit facilities to purchase Contracts, and on the availability of cash from outside sources in order to finance its continuing operations, as well as to fund the portion of Contract purchase prices not financed under revolving warehouse credit facilities. As of December 31, 2005, the Company had \$350 million in warehouse credit capacity, in the form of a \$200 million facility and a \$150 million facility. The first facility provides funding for Contracts purchased under the TFC Programs while both warehouse facilities provide funding for Contracts purchased under the CPS Programs. A third facility in the amount of \$125 million, which the Company utilized to fund Contracts under the CPS and TFC Programs was terminated by the Company on June 29, 2005.

The \$150 million warehouse facility is structured to allow CPS to fund a portion of the purchase price of Contracts by drawing against a floating rate variable funding note issued by its consolidated subsidiary Page Three Funding, LLC. This facility was established on November 15, 2005, and expires on November 14, 2006, although it is renewable with the mutual agreement of the parties. Up to 80% of the principal balance of Contracts may be advanced to the Company under this facility, subject to collateral tests and certain other conditions and covenants. Notes under this facility accrue interest at a rate of one-month LIBOR plus 2.00% per annum. At December 31, 2005, \$34.5 million was outstanding under this facility.

The \$200 million warehouse facility is similarly structured to allow CPS to fund a portion of the purchase price of Contracts by drawing against a floating rate variable funding note issued by its consolidated subsidiary Page Funding LLC. This facility was entered into on June 30, 2004. On June 29, 2005 the facility was increased from \$100 million to \$125 million and further amended to provide for funding for Contracts purchased under the TFC Programs. It was increased again to \$200 million on August 31, 2005. Approximately 77.0% of the principal balance of Contracts may be advanced to the Company under this facility, subject to collateral tests and certain other conditions and covenants. Notes under this facility accrue interest at a rate of one-month LIBOR plus 1.50% per annum. The lender has annual termination options at its sole discretion on each June 30 through 2007, at which time the agreement expires. At December 31, 2005, \$836,000 was outstanding under this facility, compared to zero at December 31, 2004.

The \$125 million warehouse facility was structured to allow the Company to fund a portion of the purchase price of Contracts by drawing against a floating rate variable funding note issued by its consolidated subsidiary CPS Warehouse Trust. This facility was established on March 7, 2002, and the maximum amount was increased to \$125 million in November 2002. Up to 73.0% of the principal balance of Contracts could have been advanced to the Company under this facility bore interest at a rate of one-month commercial paper plus 1.50% per annum. This facility was due to expire on April 11, 2006, but the Company elected to terminate it on June 29, 2005. At December 31, 2004, \$34.3 million was outstanding under this facility.

The Company securitized \$674.4 million of Contracts in five private placement transactions during the year ended December 31, 2005 compared to \$463.9 million in five private placements during 2004. All of these transactions were

structured as secured financings and, therefore, resulted in no gain on sale. In March 2004 a wholly-owned bankruptcy remote consolidated subsidiary of the Company issued \$44 million of asset-backed notes secured by its retained interest in eight term securitization transactions. The notes had an interest rate of 10% per annum and a final maturity in October 2009, were required to be repaid from the distributions on the underlying retained interests. In connection with the issuance of the notes, the Company incurred and capitalized issuance costs

F-38

---

**CONSUMER PORTFOLIO SERVICES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

of \$1.3 million. The Company repaid the notes in full in August 2005. In November 2005, the Company completed similar securitizations whereby a wholly-owned bankruptcy remote consolidated subsidiary of the Company issued \$45.8 million of asset-backed notes secured by its retained interest in term securitization transactions. These notes, which bear interest at a blended interest rate of 8.36% per annum and have a final maturity in July 2011, are required to be repaid from the distributions on the underlying retained interests. In connection with the issuance of the notes, the Company incurred and capitalized issuance costs of \$915,000.

For the portfolio owned by non consolidated subsidiaries, cash used to increase Credit Enhancement amounts to required levels for the years ended December 31, 2005, 2004 and 2003 was zero, \$2.9 million and \$20.9 million, respectively. Cash released from Trusts and their related Spread Accounts to the Company related to the portfolio owned by consolidated subsidiaries for the years ended December 31, 2005, 2004 and 2003 was \$23.1 million, \$21.4 million and \$25.9 million, respectively. Changes in the amount of Credit Enhancement required for term securitization transactions and releases from Trusts and their related Spread Accounts are affected by the relative size, seasoning and performance of the various pools of Contracts securitized that make up the Company's managed portfolio to which the respective Spread Accounts are related. During the years ended December 31, 2005 and December 31, 2004 the Company made no initial deposits to Spread Accounts and funded no initial overcollateralization related to its term securitization transactions owned by non-consolidated subsidiaries, compared to \$18.7 million in the 2003. The acquisition of Contracts for subsequent sale in securitization transactions, and the need to fund Spread Accounts and initial overcollateralization, if any, and increase Credit Enhancement levels when those transactions take place, results in a continuing need for capital. The amount of capital required is most heavily dependent on the rate of the Company's Contract purchases (other than flow purchases), the required level of initial Credit Enhancement in securitizations, and the extent to which the previously established Trusts and their related Spread Accounts either release cash to the Company or capture cash from collections on securitized Contracts. The Company is currently limited in its ability to purchase Contracts due to certain liquidity constraints. As of December 31, 2005, the Company had cash on hand of \$17.8 million and available Contract purchase commitments from its warehouse credit facilities of \$314.6 million. The Company's plans to manage the need for liquidity include the completion of additional term securitizations that would provide additional credit availability from the warehouse credit facilities, and matching its levels of Contract purchases to its availability of cash. There can be no assurance that the Company will be able to complete term securitizations on favorable economic terms or that the Company will be able to complete term securitizations at all. If the Company is unable to complete such securitizations, interest income and other portfolio related income would decrease.

The Company's primary means of ensuring that its cash demands do not exceed its cash resources is to match its levels of Contract purchases to its availability of cash. The Company's ability to adjust the quantity of Contracts that it purchases and securitizes will be subject to general competitive conditions and the continued availability of warehouse credit facilities. There can be no assurance that the desired level of Contract acquisition can be maintained or increased. While the specific terms and mechanics of each Spread Account vary among transactions, the Company's Securitization Agreements generally provide that the Company will receive excess cash flows only if the amount of Credit Enhancement has reached specified levels and/or the delinquency, defaults or net losses related to the Contracts in the pool are below certain predetermined levels. In the event delinquencies, defaults or net losses on the Contracts exceed such levels, the terms of the securitization: (i) may require increased Credit Enhancement to be accumulated for the particular pool; (ii) may restrict the distribution to the Company of excess cash flows associated with other pools; or (iii) in certain circumstances, may permit the insurers to require the transfer of servicing on some or all of the Contracts to another servicer. There can be no assurance that collections from the related Trusts will continue to generate sufficient cash.



Certain of the Company's securitization transactions and the warehouse credit facilities contain various financial covenants requiring certain minimum financial ratios and results. Such covenants include maintaining minimum levels of liquidity and net worth and not exceeding maximum leverage levels and maximum financial losses. In addition, certain securitization and non-securitization related debt contain cross-default provisions that would allow certain creditors to declare a default if a default occurred under a different facility.

F-39

---

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

The Servicing Agreements of the Company's securitization transactions are terminable by the insurers of certain of the Trust's obligations ( Note Insurers ) in the event of certain defaults by the Company and under certain other circumstances. Were a Note Insurer in the future to exercise its option to terminate the Servicing Agreements, such a termination would have a material adverse effect on the Company's liquidity and results of operations. The Company continues to receive Servicer extensions on a monthly and/or quarterly basis, pursuant to the Servicing Agreements.

**(18) Selected Quarterly Data (Unaudited)**

(in thousands, except per share data)	<b>Quarter Ended March 31,</b>	<b>Quarter Ended June 30,</b>	<b>Quarter Ended September 30,</b>	<b>Quarter Ended December 31,</b>
<b>2005</b>				
Revenues	\$ 41,833	\$ 47,776	\$ 49,374	\$ 54,714
Income (loss) before income taxes	(239 )	545	1,398	1,668
Net income (loss)	(239 )	545	1,398	1,668
Income (loss) per share:				
Basic	\$ (0.01 )	\$ 0.03	\$ 0.06	\$ 0.08
Diluted	(0.01 )	0.02	0.06	0.07
<b>2004</b>				
Revenues	\$ 27,522	\$ 32,687	\$ 34,913	\$ 37,570
Loss before income taxes	(1,407 )	(174 )	(2,061 )	(12,246 )
Net loss	(1,407 )	(174 )	(2,061 )	(12,246 )
Loss per share:				
Basic	\$ (0.07 )	\$ (0.01 )	\$ (0.10 )	\$ (0.57 )
Diluted	(0.07 )	(0.01 )	(0.10 )	(0.57 )

**CONSUMER PORTFOLIO SERVICES, INC.****UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS**

	<b>March 31, 2006</b>	<b>December 31, 2005</b>
<b>Assets</b>		
Cash and cash equivalents	\$ 25,504	\$ 17,789
Restricted cash and equivalents	212,428	157,662
Finance receivables	1,114,671	971,304
Less: Allowance for finance credit losses	(63,846 )	(57,728 )
Finance receivables, net	1,050,825	913,576
Residual interest in securitizations	22,608	25,220
Furniture and equipment, net	1,042	1,079
Deferred financing costs	9,872	8,596
Deferred tax assets, net	8,295	7,532
Accrued interest receivable	10,733	10,930
Other assets	12,916	12,760
	\$ 1,354,223	\$ 1,155,144
<b>Liabilities and shareholders equity</b>		
<b>Liabilities</b>		
Accounts payable and accrued expenses	\$ 18,721	\$ 19,568
Warehouse lines of credit	75,056	35,350
Notes payable	172	211
Residual interest financing	37,728	43,745
Securitization trust debt	1,100,606	924,026
Senior secured debt, related party	40,000	40,000
Subordinated renewable notes	6,314	4,655
Subordinated debt		14,000
	1,278,597	1,081,555
<b>Commitments and contingencies</b>		
<b>Shareholders equity</b>		
Preferred stock, \$1 par value; authorized 5,000,000 shares; none issued		
Series A preferred stock, \$1 par value; authorized 5,000,000 shares; 3,415,000 shares issued; none outstanding		
Common stock, no par value; authorized 30,000,000 shares; 21,819,333 and 21,687,584 shares issued and outstanding at March 31, 2006 and December 31, 2005, respectively	66,995	66,748
Additional paid in capital, warrants	794	794

Retained earnings	10,266	8,476
Accumulated other comprehensive loss	(2,429 )	(2,429 )
	75,626	73,589
	\$ 1,354,223	\$ 1,155,144

**See accompanying Notes to Unaudited Condensed Consolidated Financial Statements**

F-41

---

**CONSUMER PORTFOLIO SERVICES, INC.****UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

	<b>Three Months Ended March 31,</b>	
	<b>2006</b>	<b>2005</b>
<b>Revenues:</b>		
Interest income	\$ 54,527	\$ 36,172
Servicing fees	1,005	2,265
Other income	2,492	3,396
	58,024	41,833
<b>Expenses:</b>		
Employee costs	9,357	10,450
General and administrative	5,111	5,138
Interest	16,781	8,506
Interest, related party	1,254	1,878
Provision for credit losses	19,099	12,312
Marketing	3,536	2,799
Occupancy	903	782
Depreciation and amortization	193	207
	56,234	42,072
Income (loss) before income tax expense	1,790	(239 )
Income tax expense		
Net income (loss)	\$ 1,790	\$ (239 )
Earnings (loss) per share:		
Basic	\$ 0.08	\$ (0.01 )
Diluted	0.07	(0.01 )
Number of shares used in computing earnings (loss) per share:		
Basic	21,732	21,528
Diluted	24,188	21,528

**See accompanying Notes to Unaudited Condensed Consolidated Financial Statements**



**CONSUMER PORTFOLIO SERVICES, INC.****UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

	<b>Three Months Ended March 31,</b>	
	<b>2006</b>	<b>2005</b>
<b>Cash flows from operating activities:</b>		
Net income (loss)	\$ 1,790	\$ (239 )
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Amortization of deferred acquisition fees	(2,620 )	(2,614 )
Amortization of discount on Class B Notes	554	281
Depreciation and amortization	193	207
Amortization of deferred financing costs	1,242	755
Provision for credit losses	19,099	12,312
Deferred compensation		56
Releases of cash from Trusts to Company	3,943	8,010
Net deposits to Trusts to increase Spread Accounts	(6,070 )	(3,234 )
Interest income on residual assets	(961 )	(1,683 )
Cash received from residual interest in securitizations	3,573	7,980
Changes in assets and liabilities:		
Payments on restructuring accrual	(351 )	(193 )
Restricted cash	(52,638 )	(29,720 )
Accrued interest receivable	197	(406 )
Other assets	(191 )	752
Tax assets	(763 )	
Accounts payable and accrued expenses	(496 )	(1,314 )
Tax liabilities		(155 )
Net cash used in operating activities	(33,499 )	(9,205 )
<b>Cash flows from investing activities:</b>		
Purchases of finance receivables held for investment	(255,586 )	(144,165 )
Proceeds received on finance receivables held for investment	101,858	64,355
Purchase of furniture and equipment	(121 )	(22 )
Net cash used in investing activities	(153,849 )	(79,832 )
<b>Cash flows from financing activities:</b>		
Proceeds from issuance of securitization trust debt	280,977	135,924
Proceeds from issuance of retail notes payable	1,660	
Net proceeds (repayments) from warehouse lines of credit	39,706	16,256
Repayment of residual interest financing debt	(6,018 )	(5,793 )
Repayment of securitization trust debt	(104,951 )	(59,590 )
Repayment of subordinated debt	(14,000 )	(1,000 )

Edgar Filing: CONSUMER PORTFOLIO SERVICES INC - Form S-3/A

Repayment of notes payable	(40 )	(560 )
Payment of financing costs	(2,518 )	(1,094 )
Repurchase of common stock	(756 )	
Tax benefit from exercise of stock options	337	
Exercise of options and warrants	666	258
Net cash provided by financing activities	195,063	84,401
Increase (decrease) in cash	7,715	(4,636 )
Cash at beginning of period	17,789	14,366
Cash at end of period	\$ 25,504	\$ 9,730
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Interest	\$ 14,713	\$ 9,410
Income taxes	\$ 312	\$ 155

**See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.**



**CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(1) Summary of Significant Accounting Policies**

***Description of Business***

Consumer Portfolio Services, Inc. ( CPS ) was incorporated in California on March 8, 1991. CPS and its subsidiaries (collectively, the Company ) specialize primarily in purchasing, selling and servicing retail automobile installment sale contracts ( Contracts or finance receivables ) originated by licensed motor vehicle dealers located throughout the United States ( Dealers ) in the sale of new and used automobiles, light trucks and passenger vans. Through its purchases, the Company provides indirect financing to Dealer customers for borrowers with limited credit histories, low incomes or past credit problems ( Sub-Prime Customers ). The Company serves as an alternative source of financing for Dealers, allowing sales to customers who otherwise might not be able to obtain financing. The Company does not lend money directly to consumers. Rather, it purchases installment Contracts from Dealers based on its financing programs (the CPS Programs ).

***Basis of Presentation***

The Unaudited Condensed Consolidated Financial Statements of the Company have been prepared in conformity with accounting principles generally accepted in the United States of America, with the instructions to Form 10-Q and with Article 10 of Regulation S-X of the Securities and Exchange Commission, and include all adjustments that are, in the opinion of management, necessary for a fair presentation of the results for the interim periods presented. All such adjustments are, in the opinion of management, of a normal recurring nature. In addition, certain items in prior period financial statements may have been reclassified for comparability to current period presentation. Results for the three-month period ended March 31, 2006 are not necessarily indicative of the operating results to be expected for the full year.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted from these Unaudited Condensed Consolidated Financial Statements. These Unaudited Condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and Notes to Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2005.

***Other Income***

Other Income consists primarily of recoveries on previously charged off MFN contracts and fees paid to the Company by Dealers for certain direct mail services the Company provides. The recoveries on the charged-off MFN contracts were \$937,000 and \$1.6 million for the three months ended March 31, 2006 and 2005, respectively. The direct mail revenues were \$897,000 and \$1.2 million for the same periods in 2006 and 2005, respectively.

***Stock-based Compensation***

Effective January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123(R), Share-Based Payment, revised 2004 (SFAS 123R ), prospectively for all option awards granted, modified or settled after January 1, 2006 using the modified prospective method. Under this method, the Company recognizes compensation costs in the financial statements for all share-based payments granted subsequent to January 1, 2006 based on the grant date fair value estimated in accordance with the provisions of SFAS 123(R). Results for prior periods have not been restated.

For the three months ended March 31, 2006, the Company recorded no stock-based compensation costs as there were no option awards granted during the three-month period ended March 31, 2006 and there was no vesting of option awards for options granted prior to January 1, 2006 since all options outstanding as of December 31, 2005 were fully vested at that time. As of March 31, 2006, there are no unrecognized stock-based compensation costs to be recognized over future periods.

F-44

---

## CONSUMER PORTFOLIO SERVICES, INC.

## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The following represents stock option activity for the three months ended March 31, 2006:

	Number of Shares (in thousands)	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term
Options outstanding at the beginning of period	4,864	\$ 3.38	
Granted			
Exercised	(251 )	2.66	
Forfeited	(4 )	3.27	
Options outstanding at the end of period	4,609	\$ 3.42	7.33 years
Options exercisable at the end of period	4,609	\$ 3.42	7.33 years

At March 31, 2006 the aggregate intrinsic value of options outstanding and exercisable was \$22.0 million. The total intrinsic value of options exercised was \$1.0 million and \$399,000 for the three months ended March 31, 2006 and 2005, respectively. New shares were issued for all options exercised during the three-month periods ended March 31, 2006 and 2005. There were 169,261 shares available for future stock option grants under existing plans as of March 31, 2006.

Prior to January 1, 2006, as was permitted by Statement of Financial Accounting Standards No. 123, Accounting for Stock-Based Compensation ( SFAS No. 123 ), the Company accounted for stock-based employee compensation plans in accordance with Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees and related interpretations, whereby stock options are recorded at intrinsic value equal to the excess of the share price over the exercise price at the date of grant. The Company provided the pro forma net income (loss), pro forma earnings (loss) per share, and stock based compensation plan disclosure requirements set forth in SFAS No. 123. The Company accounted for repriced options as variable awards.

Compensation cost was recognized for certain stock options in the Unaudited Condensed Consolidated Financial Statements in accordance with APB Opinion No. 25. Had the Company determined compensation cost based on the fair value at the grant date for its stock options under Statement of Financial Accounting Standards No. 123 ( SFAS 123 ), Accounting for Stock Based Compensation, the Company's net (loss) and (loss) per share would have been increased to the pro forma amounts indicated below.

(in thousands, except per share data)	Three Months Ended March 31, 2005
Net (loss), as reported	\$ (239 )
Stock-based employee compensation expense, fair value method, net of tax	(200 )
Previously recorded stock-based employee compensation expense, intrinsic value method, net of tax	32
Pro forma net (loss)	\$ (407 )

Net (loss) per share		
Basic, as reported	\$	(0.01 )
Diluted, as reported	\$	(0.01 )
Pro forma Basic	\$	(0.02 )
Pro forma Diluted	\$	(0.02 )

F-45

---

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

The Company uses the Black-Scholes-Merton option valuation model to estimate the fair value of each option on the date of grant using the assumptions noted in the following table. The Company utilizes assumptions on expected life, risk-free rate, expected volatility, and dividend yield to determine such values. The Company did not disclose assumptions for the three months ended March 31, 2006 because there were no options granted in the period. The expected term of options granted is derived from historical data on employee exercise and post-vesting termination behavior. The risk-free rate is based on treasury instruments in effect at the time of grant whose terms are consistent with the expected term of the Company's stock options. Expected volatility is based on historical volatility of the Company's stock. The dividend yield is based on historical experience and expected future changes.

The Company uses the Black-Scholes-Merton option valuation model to estimate the fair value of each option on the date of grant using the assumptions noted in the following table. The Company utilizes assumptions on expected life, risk-free rate, expected volatility, and dividend yield to determine such values. The Company did not disclose assumptions for the three months ended March 31, 2006 because there were no options granted in the period. The expected term of options granted is derived from historical data on employee exercise and post-vesting termination behavior. The risk-free rate is based on treasury instruments in effect at the time of grant whose terms are consistent with the expected term of the Company's stock options. Expected volatility is based on historical volatility of the Company's stock. The dividend yield is based on historical experience and expected future changes.

	<b>Three Months Ended March 31, 2005</b>
Risk-free interest rate	4.30 %
Expected term, in years	6.5
Expected volatility	52.53 %
Dividend yield	0 %

***Purchases of Company Stock***

During the three-month periods ended March 31, 2006 and 2005, the Company purchased 118,751 and zero shares, respectively, of its common stock. The shares purchased during the three-month period ended March 31, 2006 were purchased at an average price of \$6.37.

***New Accounting Pronouncements***

In March 2006, the FASB issued FASB Statement No. 156, Accounting for the Servicing of Financial Assets an Amendment to FASB Statement No. 140 (FAS 156). With respect to the accounting for separately recognized servicing assets and servicing liabilities, this statement: (1) requires an entity to recognize a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a specific types of servicing contracts identified in the statement, (2) requires that all separately recognized servicing assets and servicing liabilities to be initially measured at fair value, if practicable, (3) permits an entity to choose subsequent measurement methods for each class of separately recognized servicing assets and servicing liabilities, (4) permits a one-time

reclassification of available-for-sale securities to trading securities by entities with recognized servicing rights at the initial adoption of this statement, and (5) requires a separate presentation of servicing assets and servicing liabilities subsequently measured at fair value in the statement of financial position and additional disclosures for all separately recognized servicing assets and servicing liabilities. FAS 156 will be effective for the Company on January 1, 2007. The Company is currently in the process of evaluating the effects of this Standard, but does not believe it will have a significant effect on its financial position or results of operations.

F-46

---

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(2) Finance Receivables**

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

(in thousands)	<b>March 31, 2006</b>	<b>December 31, 2005</b>
Finance Receivables		
Automobile		
Simple Interest	\$ 1,087,048	\$ 933,510
Pre-compute, net of unearned interest	46,882	54,693
Finance Receivables, net of unearned interest	1,133,930	988,203
Less: Unearned acquisition fees and originations costs	(19,259 )	(16,899 )
Finance Receivables	\$ 1,114,671	\$ 971,304

The following table presents a summary of the activity for the allowance for credit losses for the three-month periods ended March 31, 2006 and 2005:

(in thousands)	<b>March 31, 2006</b>	<b>March 31, 2005</b>
Balance at beginning of period	\$ 57,728	\$ 42,615
Provision for credit losses on finance receivables	19,099	12,312
Recoveries	(19,235 )	(11,436 )
Charge offs	6,254	2,793
Balance at end of period	\$ 63,846	\$ 46,284

**(3) Residual Interest in Securitizations**

The residual interest in securitizations represents the discounted sum of expected future cash flows from securitization trusts. The following table presents the components of the residual interest in securitizations and are shown at their discounted amounts:

(in thousands)	<b>March 31, 2006</b>	<b>December 31, 2005</b>
Cash, commercial paper, United States government securities and other qualifying investments (Spread Accounts)	\$ 13,201	\$ 12,748
Receivables from Trusts (NIRs)	3,913	5,798
Overcollateralization	5,494	6,674
Residual interest in securitizations	\$ 22,608	\$ 25,220

F-47

---



**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

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

(dollars in thousands)	<b>March 31, 2006</b>	<b>December 31, 2005</b>
Undiscounted estimated credit losses	\$ 4,648	\$ 5,724
Managed portfolio held by non-consolidated subsidiaries	83,162	103,130
Undiscounted estimated credit losses as percentage of managed portfolio held by non-consolidated subsidiaries	5.6%	5.6%

The key economic assumptions used in measuring all residual interest in securitizations as of March 31, 2006 and December 31, 2005 are included in the table below. The pre-tax discount rate remained constant from previous periods at 14%, except for certain cash flows from charged off receivables related to the Company's securitizations from 2001 to 2003 where the Company has used a discount rate of 25%, which is also consistent with previous periods.

	<b>March 31, 2006</b>	<b>December 31, 2005</b>
Prepayment speed (Cumulative)	22.2% - 35.3%	22.2% - 35.8%
Net credit losses (Cumulative)	12.3% - 20.0%	11.9% - 20.2%

## CONSUMER PORTFOLIO SERVICES, INC.

## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

## (4) Securitization Trust Debt

The Company has completed a number of securitization transactions that are structured as secured borrowings for financial accounting purposes. The debt issued in these transactions is shown on the Company's Unaudited Condensed Consolidated Balance Sheets as Securitization Trust Debt, and the components of such debt are summarized in the following table:

Series	Final Scheduled Payment Date (1)	Receivables Pledged at March 31, 2006	Initial Principal	Outstanding Principal at March 31, 2006	Outstanding Principal at December 31, 2005	Weighted Average Interest Rate at March 31, 2006
MFN						
2001-A	June 2007	\$	\$ 301,000	\$	\$	N/A
TFC 2002-1	August 2007		64,552			N/A
TFC 2002-2	March 2008		62,589			N/A
TFC 2003-1	January 2009	5,413	52,365	4,741	6,557	2.69%
CPS						
2003-C	March 2010	26,859	87,500	25,835	30,550	3.57%
CPS						
2003-D	October 2010	26,481	75,000	25,384	29,688	3.81%
CPS						
2004-A	October 2010	34,626	82,094	34,695	40,225	3.84%
PCR 2004-1	March 2010	21,361	76,257	17,671	22,873	3.80%
CPS						
2004-B	February 2011	46,279	96,369	46,394	52,704	4.17%
CPS						
2004-C	April 2011	54,594	100,000	54,507	61,779	3.95%
CPS						
2004-D	December 2011	73,473	120,000	72,530	82,801	4.44%
CPS						
2005-A	October 2011	96,983	137,500	97,113	110,021	5.11%
CPS						
2005-B	February 2012	109,360	130,625	107,749	113,194	4.56%
CPS						
2005-C	March 2012	172,025	183,300	169,778	173,509	5.00%
CPS						
2005-TFC	July 2012	71,941	72,525	62,432	72,525	5.79%
	July 2012	138,293	145,000	136,777	127,600	5.63%

CPS						
2005-D						
CPS						
2006-A (2)	November 2012	142,446	245,000	245,000		5.87%
		\$ 1,020,134	\$ 2,031,676	\$ 1,100,606	\$ 924,026	

The Final Scheduled Payment Date represents final legal maturity of the securitization trust debt. Securitization trust debt is expected to become due and to be paid prior to those dates, based on amortization of the finance receivables pledged to the Trusts. Expected payments, which will depend on the performance of such receivables, as to which there can be no assurance, are \$290.2 million in 2006, \$289.8 million in 2007, \$211.1 million in 2008, \$154.6 million in 2009, \$110.6 million in 2010 and \$44.4 million in 2012.

Receivables Pledged at March 31, 2006 excludes approximately \$100.7 million in Contracts delivered to this Trust in April 2006 pursuant to a pre-funding structure.

All of the securitization trust debt was sold in private placement transactions to qualified institutional buyers. The debt was issued through wholly-owned bankruptcy remote subsidiaries of CPS, TFC or MFN, and is secured by the assets of such subsidiaries, but not by other assets of the Company. Principal of \$1.0 billion, and the related interest payments, are guaranteed by financial guaranty insurance policies issued by third party financial institutions.

The terms of the various Securitization Agreements related to the issuance of the securitization trust debt and the warehouse credit facilities require that certain delinquency and credit loss criteria be met with respect to the collateral pool, and require that the Company maintain minimum levels of liquidity and net worth and not exceed maximum leverage levels and maximum financial losses. In addition, certain securitization and non-securitization related debt contain cross-default provisions, which would allow certain creditors to declare a default if a default were declared under a different facility. As of March 31, 2006, the Company was in compliance with all such financial covenants.

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

The Company is responsible for the administration and collection of the Contracts. The Securitization Agreements also require certain funds be held in restricted cash accounts to provide additional collateral for the borrowings or to be applied to make payments on the securitization trust debt. As of March 31, 2006, restricted cash under the various agreements totaled approximately \$212.4 million. Interest expense on the securitization trust debt is composed of the stated rate of interest plus amortization of additional costs of borrowing. Additional costs of borrowing include facility fees, insurance and amortization of deferred financing costs. Deferred financing costs related to the securitization trust debt are amortized using a level yield method. Accordingly, the effective cost of borrowing of the securitization trust debt is greater than the stated rate of interest.

The wholly-owned, bankruptcy remote subsidiaries of CPS, MFN and TFC were formed to facilitate the above asset-backed financing transactions. Similar bankruptcy remote subsidiaries issue the debt outstanding under the Company's warehouse lines of credit. Bankruptcy remote refers to a legal structure in which it is expected that the applicable entity would not be included in any bankruptcy filing by its parent or affiliates. All of the assets of these subsidiaries have been pledged as collateral for the related debt. All such transactions, treated as secured financings for accounting and tax purposes, are treated as sales for all other purposes, including legal and bankruptcy purposes. None of the assets of these subsidiaries are available to pay other creditors of the Company or its affiliates.

**(5) Interest Income**

The following table presents the components of interest income:

	<b>Three Months Ended March 31,</b>	
	<b>2006</b>	<b>2005</b>
Interest on Finance Receivables	\$ 52,360	\$ 33,985
Residual interest income	961	1,683
Other interest income	1,206	504
Net interest income	\$ 54,527	\$ 36,172

**(6) Earnings (Loss) Per Share**

Earnings (loss) per share for the three-month periods ended March 31, 2006 and 2005 were calculated using the weighted average number of shares outstanding for the related period. The following table reconciles the number of shares used in the computations of basic and diluted earnings (loss) per share for the three-month periods ended March 31, 2006 and 2005:

	<b>Three Months Ended March 31,</b>	
(in thousands)	<b>2006</b>	<b>2005</b>
Weighted average number of common shares outstanding during the period used to compute basic earnings (loss) per share	\$ 21,732	\$ 21,528
Incremental common shares attributable to exercise of outstanding options and warrants	2,456	

Weighted average number of common shares used to compute diluted earnings (loss) per share	\$ 24,188	\$ 21,528
--	-----------	-----------

If the anti-dilutive effects of common stock equivalents were considered, additional shares included in the diluted earnings (loss) per share calculation for the three-month period ended March 31, 2005 would have included an additional 2.0 million shares attributable to the exercise of outstanding options and warrants. No such anti-dilution adjustment was applicable to the three-month period ended March 31, 2006.

F-50

---

**CONSUMER PORTFOLIO SERVICES, INC.**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(7) Income Taxes**

As of December 31, 2005, the Company had net deferred tax assets of \$7.5 million, which included a valuation allowance of \$43.7 million against gross deferred tax assets of \$53.1 million. There were also offsetting gross deferred tax liabilities of \$1.8 million. Net tax assets at March 31, 2006 were \$8.3 million compared with net tax assets at December 31, 2005 of \$7.5 million. The Company decreased its valuation allowance by the income tax expense for the period to result in no net income tax provision for the three-month period ended March 31, 2006. The Company has evaluated its deferred tax assets and believes that it is more likely than not that certain deferred tax assets will not be realized due to limitations imposed by the Internal Revenue Code and expected future taxable income.

**(8) Legal Proceedings**

*Stanwich Litigation.* CPS was for some time a defendant in a class action (the Stanwich Case ) brought in the California Superior Court, Los Angeles County. The original plaintiffs in that case were persons entitled to receive regular payments (the Settlement Payments ) under out-of-court settlements reached with third party defendants. Stanwich Financial Services Corp. ( Stanwich ), an affiliate of the former chairman of the board of directors of CPS, is the entity that was obligated to pay the Settlement Payments. Stanwich has defaulted on its payment obligations to the plaintiffs and in June 2001 filed for reorganization under the Bankruptcy Code, in the federal Bankruptcy Court of Connecticut. At December 31, 2004, CPS was a defendant only in a cross-claim brought by one of the other defendants in the case, Bankers Trust Company, which asserted a claim of contractual indemnity against CPS.

CPS subsequently settled the cross-claim of Bankers Trust by payment of \$3.24 million, on or about February 8, 2005. Pursuant to that settlement, the court has dismissed the cross-claim, with prejudice. The amount paid by the Company was accrued for and included in Accounts payable and accrued expenses in the Company's balance sheet as of December 31, 2004.

In November 2001, one of the defendants in the Stanwich Case, Jonathan Pardee, asserted claims for indemnity against the Company in a separate action, which is now pending in federal district court in Rhode Island. The Company has filed counterclaims in the Rhode Island federal court against Mr. Pardee, and has filed a separate action against Mr. Pardee's Rhode Island attorneys, in the same court. The action of Mr. Pardee against CPS is stayed, awaiting resolution of an adversary action brought against Mr. Pardee in the bankruptcy court, which is hearing the bankruptcy of Stanwich.

The reader should consider that any adverse judgment against CPS in the Stanwich Case (or the related case in Rhode Island) for indemnification, in an amount materially in excess of any liability already recorded in respect thereof, could have a material adverse effect on the Company's financial position.

*Other Litigation.* On June 2, 2004, Delmar Coleman filed a lawsuit in the circuit court of Tuscaloosa, Alabama, alleging that plaintiff Coleman was harmed by an alleged failure to refer, in the notice given after repossession of his vehicle, to the right to purchase the vehicle by tender of the full amount owed under the retail installment contract. Plaintiff seeks damages in an unspecified amount, on behalf of a purported nationwide class. CPS removed the case to federal bankruptcy court, and filed a motion for summary judgment as part of its adversary proceeding against the plaintiff in the bankruptcy court. The federal bankruptcy court granted the plaintiff's motion to send the matter back to Alabama state court. CPS appealed the ruling, and the federal district court, in which the appeal was heard, has since ordered the bankruptcy court to decide whether the plaintiff has standing to pursue her claims, and, if standing is found, to reconsider its remand decision. It is possible that plaintiff may in turn appeal from the order of the district court. Although CPS believes that it has one or more defenses to each of the claims made in this lawsuit, no discovery

has yet been conducted and the case remains in its earliest stages. Accordingly, there can be no assurance as to its outcome.

F-51

---

**CONSUMER PORTFOLIO SERVICES, INC.****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

In June 2004, Plaintiff Jeremy Henry filed a lawsuit against the Company in the California Superior Court, San Diego County, alleging improper practices related to the notice given after repossession of a vehicle that he purchased. Plaintiff's motion for a certification of a class has been denied, and is the subject of an appeal now before the California Court of Appeal. Irrespective of the outcome of that appeal, as to which there can be no assurance, the Company has a number of defenses that may be asserted with respect to the claims of plaintiff Henry.

In August and September 2005, two plaintiffs represented by the same law firm filed substantially identical lawsuits in the federal district court for the northern district of Illinois, each of which purports to be a class action, and each of which alleges that CPS improperly accessed consumer credit information. CPS has reached agreements in principle to settle these cases, which await confirmation by the court.

The Company has recorded a liability as of March 31, 2006 that it believes represents a sufficient allowance for legal contingencies, including those described above. Any adverse judgment against the Company, if in an amount materially in excess of the recorded liability, could have a material adverse effect on the financial position of the Company.

The Company is routinely involved in various legal proceedings resulting from its consumer finance activities and practices, both continuing and discontinued. The Company believes that there are substantive legal defenses to such claims, and intends to defend them vigorously. There can be no assurance, however, as to the outcome.

**(9) Employee Benefits**

The Company sponsors the MFN Financial Corporation Benefit Plan (the Plan). Plan benefits were frozen September 30, 2001. The table below sets forth the Plan's net periodic benefit cost for the three months ended March 31, 2006 and 2005.

	<b>Three Months Ended March 31,</b>	
	<b>2006</b>	<b>2005</b>
<b>Components of net periodic benefit cost</b>		
Service cost	\$	\$
Interest Cost	213	211
Expected return on assets	(287)	(292)
Amortization of transition (asset)/obligation	(2)	(9)
Amortization of net (gain) / loss	34	12
Net periodic benefit cost	\$ (42)	\$ (78)

**(10) Comprehensive Income (Loss)**

The components of comprehensive income (loss) are as follows:

**Three Months Ended  
March 31,**



Edgar Filing: CONSUMER PORTFOLIO SERVICES INC - Form S-3/A

	<b>2006</b>		<b>2005</b>
Net income (loss)	\$ 1,790	\$	(239 )
Minimum pension liability, net of tax			(185 )
Comprehensive income (loss)	\$ 1,790	\$	(424 )

F-52

---



**PART II****INFORMATION NOT REQUIRED IN PROSPECTUS****Item 14. Other Expenses of Issuance and Distribution**

Set forth below are expenses (other than the selling agent's commissions and expenses) expected to be incurred in connection with the issuance and distribution of the securities registered hereby. With the exception of the Securities and Exchange Commission registration fee and the NASD filing fee, the amounts set forth below are estimates and actual expenses may vary considerably from these estimates depending upon how long the notes are offered and other factors:

Securities and Exchange Commission registration fee	\$ 3,730
NASD filing fee	3,700
Accounting fees and expenses	50,000
Blue Sky fees and expenses	
Legal fees and expenses	50,000
Printing expenses	15,000
Selling shareholders' counsel fees and expenses	25,000
Miscellaneous	22,570
Total	\$ 170,000

**Item 15. Indemnification of Directors and Officers**

Under California law, a California corporation may eliminate or limit the personal liability of a director of the corporation for monetary damages for breach of the director's duty of care as a director, provided that the breach does not involve certain enumerated actions, including, among other things, intentional misconduct or knowing and culpable violation of the law, acts or omissions which the director believes to be contrary to the best interests of the corporation or its shareholders or which reflect an absence of good faith on the director's part, the unlawful purchase or redemption of stock, payment of unlawful dividends, and receipt of improper personal benefits. The registrant's Board of Directors believes that such provisions have become commonplace among major corporations and are beneficial in attracting and retaining qualified directors, and the registrant's Articles of Incorporation include such provisions.

The registrant's Articles of Incorporation and Bylaws also impose a mandatory obligation upon the registrant to indemnify any director or officer to the fullest extent authorized or permitted by law (as now or hereinafter in effect), including under circumstances in which indemnification would otherwise be at the discretion of the registrant.

In the form of underwriting agreement to be filed as Exhibit 1.1 to this Registration Statement, it is anticipated that the underwriter will agree to indemnify, under certain conditions, the registrant, its officers and directors, and persons who control the registrant within the meaning of the Securities Act of 1933, as amended, against certain liabilities.

**Item 16. Exhibits and Financial Statement Schedules**

<b>Exhibit No.</b>	<b>Description</b>
*1.1	Form of Underwriting Agreement
*5.1	Opinion of Andrews Kurth LLP with respect to legality of the securities registered
*23.1	Consent of Andrews Kurth LLP (included in Exhibit 5.1)
23.2	Consent of McGladrey & Pullen LLP

23.3

Consent of KPMG LLP

\*

To be filed by amendment

II-1

---

**Item 17. Undertakings**

The undersigned registrant hereby undertakes:

(a) That, for purposes of determining any liability under the Securities Act, the undersigned registrant undertakes that each filing of an annual report of the undersigned registrant pursuant to section 13(a) or section 15(d) of the Exchange Act (and, where applicable, each filing of an employee benefit plan's annual report pursuant to section 15(d) of the Exchange Act) that is incorporated by reference in this registration statement shall be deemed to be a new registration statement relating to the securities offered herein, and the offering of such securities at that time shall be deemed to be the initial bona fide offering thereof.

(b) Insofar as indemnification for liabilities arising under the Securities Act of 1933 may be permitted to directors, officers and controlling persons of the registrant pursuant to the provisions described under Item 15 above, or otherwise, the registrant has been advised that in the opinion of the Securities and Exchange Commission such indemnification is against public policy as expressed in the Securities Act of 1933 and is, therefore, unenforceable. In the event that a claim for indemnification against such liabilities (other than the payment by the registrant of expenses incurred or paid by a director, officer or controlling person of the registrant in the successful defense of any action, suit or proceeding) is asserted by such director, officer or controlling person in connection with the securities being registered, the registrant will, unless in the opinion of its counsel the matter has been settled by controlling precedent, submit to a court of appropriate jurisdiction the question whether such indemnification by it is against public policy as expressed in the Securities Act of 1933 and will be governed by the final adjudication of such issue.

(c) For purposes of determining any liability under the Securities Act, the information omitted from the form of Prospectus filed as part of this Registration Statement in reliance upon Rule 430A and contained in a form of prospectus filed by us pursuant to Rule 424(b)(1) or (4) or 497(h) under the Securities Act shall be deemed to be part of this Registration Statement as of the time it was declared effective; and

(d) For the purpose of determining any liability under the Securities Act, each post-effective amendment that contains a form of Prospectus shall be deemed to be a new Registration Statement relating to the securities offered therein and the offering of such securities at the time shall be deemed to be the initial bona fide offering thereof.

**SIGNATURES**

Pursuant to the requirements of the Securities Act of 1933, the registrant certifies that it has reasonable grounds to believe that it meets all of the requirements for filing on Form S-3 and has duly caused this Registration Statement on Form S-3 to be signed on its behalf by the undersigned, thereunto duly authorized, in Irvine, State of California, on July 18, 2006.

CONSUMER PORTFOLIO SERVICES, INC.

By: /s/ Charles E. Bradley, Jr.  
Charles E. Bradley, Jr.,  
President and Chief Executive Officer

**POWER OF ATTORNEY**

Pursuant to the requirements of the Securities Act of 1933, as amended, this Registration Statement on Form S-3 has been signed by the following persons in the capacities and on the dates indicated below.

<b>Signature</b>	<b>Title</b>	<b>Date</b>
/s/ Charles E. Bradley, Jr. Charles E. Bradley, Jr.	Chairman of the Board of Directors, President, and Chief Executive Officer (Principal Executive Officer)	July 18, 2006
/s/ Jeffrey P. Fritz Jeffrey P. Fritz	Sr. Vice President (Principal Financial and Accounting Officer)	July 18, 2006
* E. Bruce Fredrikson	Director	July 18, 2006
John E. McConnaughy	Director	
* John G. Poole	Director	July 18, 2006
* William B. Roberts	Director	July 18, 2006
* John C. Warner	Director	July 18, 2006
* Daniel S. Wood	Director	July 18, 2006

\* By: /s/ Jeffrey P. Fritz  
Jeffrey P. Fritz,  
Attorney-in-Fact

July 18, 2006

II-3

---

**EXHIBIT INDEX**

<b>Exhibit No.</b>	<b>Description</b>
1.1 *	Form of Underwriting Agreement
5.1 *	Opinion of Andrews Kurth LLP with respect to legality of the securities registered
23.1 *	Consent of Andrews Kurth LLP (included in Exhibit 5.1)
23.2	Consent of McGladrey & Pullen LLP
23.3	Consent of KPMG LLP

\*

To be filed by amendment