

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

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

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

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

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

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

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

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

The collections industry is heavily regulated under various federal, state and local laws, rules and regulations. Many states and several cities require that we be licensed as a debt collection company. The Federal Trade Commission, state Attorneys General and other regulatory bodies have the authority to investigate a variety of

matters including consumer complaints against debt collection companies and to recommend enforcement actions and seek monetary penalties. If we or our third party collection agencies or law firms fail to comply with applicable laws, rules and regulations, including, but not limited to, identity theft, privacy, data security, the use of automated dialing equipment, laws related to consumer protection, debt collection, and laws applicable to specific types of debt, it could result in the suspension or termination of our ability to conduct collection operations, which would materially adversely affect us. Furthermore, our ability to collect may be impacted by state laws which require that certain types of account documentation be in our possession prior to the institution of any collection activities. In addition, new federal, state or local laws or regulations, or changes in the ways these rules or laws are interpreted or enforced, could limit our activities in the future and/or significantly increase the cost of regulatory compliance.

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

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

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

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

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

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

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

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

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

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

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

Securities class-action litigation has often been filed against companies after a period of volatility in the market price of their stock. Our industry experiences a high volume of litigation, and legal precedents have not been clearly established in many areas applicable to our business. Additionally, employment-related litigation is

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

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

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

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

Our management team has considerable experience in finance, banking, consumer collections and other industries. We believe that the expertise of our executives obtained by managing businesses across numerous other industries has been critical to the enhancement of our operations. Our management team has created a culture of new ideas and progressive thinking, coupled with increased use of technology and statistical analysis. The loss of the

services of one or more of our key executive officers could disrupt our operations and seriously impair our ability to continue to acquire or collect on portfolios of charged-off consumer receivables and to manage and expand our business. Our success depends on the continued service and performance of our management team, and we cannot guarantee that we will be able to retain such individuals.

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

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

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

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

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

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

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

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

Our business relies on computer and telecommunications technologies, and our ability to integrate new technologies into our business is essential to our competitive position and our success. We may not be successful in

anticipating, managing, or adopting technological changes in a timely basis. Computer and telecommunications technologies are evolving rapidly and are characterized by short product life cycles.

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

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

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

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

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

Our business model may be uniquely vulnerable to an economic recession, which typically results in an increase in the amount of defaulted consumer receivables, thereby contributing to an increase in the amount of personal bankruptcy filings. Under certain bankruptcy filings, a consumer's assets are sold to repay credit

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

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

### **Item 1B—Unresolved Staff Comments**

None.

### **Item 2—Properties**

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

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

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

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

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

### **Item 3—Legal Proceedings**

On October 18, 2004, Timothy W. Moser, one of our former officers, filed an action in the United States District Court for the Southern District of California against us, and certain individuals, including several of our officers and directors. On February 14, 2005, we were served with an amended complaint in this action alleging defamation, intentional interference with contractual relations, breach of contract, breach of the covenant of good faith and fair dealing, intentional and negligent infliction of emotional distress and civil conspiracy arising out of certain statements in our Registration Statement on Form S-1, originally filed in September 2003, and alleged to be included in our Registration Statement on Form S-3, originally filed in May 2004. The amended complaint sought injunctive relief, economic and punitive damages in an unspecified amount plus an award of profits

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allegedly earned by the defendants and alleged co-conspirators as a result of the alleged conduct, in addition to attorney's fees and costs. On June 1, 2006, the plaintiff filed a second amended complaint in which he amended his claim for negligent infliction of emotional distress. On January 19, 2010, the District Court issued an order granting defendants' summary judgment motions, dismissed all causes of action against all of the defendants and entered judgment in favor of the defendants. On February 12, 2010, Mr. Moser filed a notice of appeal of the judgment. The parties are in the process of briefing their arguments on appeal and no date for oral argument has been set.

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

We, along with others in our industry, are routinely subject to legal actions based on the Fair Debt Collection Practices Act, or FDCPA, comparable state statutes and common law causes of action. The violations of law alleged in these actions often include claims that we lack specified licenses to conduct our business, attempt to collect debts on which the statute of limitations has run, and/ or have made inaccurate assertions of fact in support of our

collection actions. A number of these cases are styled as class actions and a class has been certified in several of these cases. Many of these cases present novel issues on which there is no clear legal precedent.

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

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

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

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

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

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

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

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

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