CREDIT ACCEPTANCE CORPORATION
Form 10-K
March 02, 2007

Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-K

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

For the Fiscal Year Ended December 31, 2006

Commission File Number 000-20202

CREDIT ACCEPTANCE CORPORATION
(Exact Name of Registrant as Specified in its Charter)

Michigan	**38-1999511**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
25505 W. Twelve Mile Road, Suite 3000 Southfield, Michigan	**48034-8339**
(Address of Principal Executive Offices)	(Zip Code)

Registrant s telephone number, including area code: (248) 353-2700
Securities Registered Pursuant to Section 12(b) of the Act:
Common Stock
Securities Registered Pursuant to Section 12(g) of the Act:
None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No þ

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No þ

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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

Large accelerated filer o Accelerated filer þ Non-accelerated filer o

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

The aggregate market value of 5,027,759 shares of the Registrant s common stock held by non-affiliates on June 30, 2006 was approximately $136.5 million. For purposes of this computation all officers, directors and 10% beneficial owners of the Registrant are assumed to be affiliates. Such determination should not be deemed an admission that such officers, directors and beneficial owners are, in fact, affiliates of the Registrant.

At February 28, 2007, there were 30,250,187 shares of the Registrant s common stock issued and outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant s definitive Proxy Statement pertaining to the 2007 Annual Meeting of Shareholders (the Proxy Statement) filed pursuant to Regulation 14A are incorporated herein by reference into Part III.

CREDIT ACCEPTANCE CORPORATION
YEAR ENDED DECEMBER 31, 2006
INDEX TO FORM 10-K

Item		Page
	PART I	
1.	Business	3
1A.	Risk Factors	12
1B.	Unresolved Staff Comments	14
2.	Properties	14
3.	Legal Proceedings	14
4.	Submission of Matters to a Vote of Security Holders	14
	PART II	
5.	Market for Registrant s Common Equity and Related Stockholder Matters	15
6.	Selected Financial Data	19
7.	Management s Discussion and Analysis of Financial Condition and Results of Operations	20
7A.	Quantitative and Qualitative Disclosures About Market Risk	33
8.	Financial Statements and Supplementary Data	34
9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	70
9A.	Controls and Procedures	70
	PART III	
10.	Directors, Executive Officers and Corporate Governance	72
11.	Executive Compensation	72
12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	72
13.	Certain Relationships and Related Transactions, and Director Independence	72
14.	Principal Accountant Fees and Services	72
	PART IV	

15. Exhibits and Financial Statement Schedules 73

Amendment No. 1, dated July 24, 2006, to First Amended and Restated Loan and Security Agreement
Amendment No. 2 to First Amended and Restated Loan and Security Agreement
Schedule of Credit Acceptance Corporation Subsidiaries
Consent of Grant Thornton LLP
Certification of Chief Executive Officer Pursuant to Rule 13a-14(a)
Certification of Chief Financial Officer Pursuant to Rule 13a-14(a)
Certification of Chief Executive Officer Pursuant to Section 906
Certification of Chief Financial Officer Pursuant to Section 906

Table of Contents

PART I

ITEM 1. BUSINESS

General

Since 1972, Credit Acceptance (the Company or Credit Acceptance) has provided auto loans to consumers, regardless of their credit history. The Company s product is offered through a nationwide network of automobile dealers who benefit from sales of vehicles to consumers who otherwise could not obtain financing; from repeat and referral sales generated by these same customers; and from sales to customers responding to advertisements for the Company s product, but who actually end up qualifying for traditional financing.

Without the Company s product, consumers are often unable to purchase a vehicle or they purchase an unreliable one and are not provided the opportunity to improve their credit standing. As the Company reports to the three national credit reporting agencies, a significant number of its consumers improve their lives by improving their credit score and move on to more traditional sources of financing.

Credit Acceptance was founded to collect retail installment contracts (referred to as Consumer Loans) originated by automobile dealerships owned by the Company s founder, majority shareholder, and current Chairman, Donald Foss. During the 1980s, the Company began to market this service to non-affiliated dealers and, at the same time, began to offer dealers a non-recourse cash payment (referred to as an advance) against anticipated future collections on Consumer Loans serviced for that dealer. Today, the Company s program is offered to dealers throughout the United States. The Company refers to dealers who participate in its program and who share its commitment to changing consumers lives as dealer-partners .

The Company s Internet address is *creditacceptance.com*. The Company makes available, free of charge on the web site, copies of reports it files with or furnishes to the Securities and Exchange Commission as soon as reasonably practicable after the Company electronically files or furnishes such reports.

The Company is an indirect lender from a legal perspective, meaning the Consumer Loan is originated by the dealer-partner and immediately assigned to the Company. Typically, the compensation paid to the dealer-partner in exchange for the Consumer Loan is paid in two parts. A portion of the compensation is paid at the time of origination, and a portion is paid over time. The amount paid at the time of origination is called an advance; the portion paid over time is based on the performance of the loan and is called dealer holdback.

For accounting purposes, the transactions described above are not considered to be loans to consumers. Instead, the Company s accounting reflects that of a lender to the dealer-partner. This classification for accounting purposes is primarily a result of (i) the dealer-partner s financial interest in the Consumer Loan and (ii) certain elements of the Company s legal relationship with the dealer-partner. The cash amount advanced to the dealer-partner is recorded as an asset on the Company s balance sheet. The aggregate amount of all advances to an individual dealer-partner, plus accrued income, less repayments comprises the amount recorded in Loans receivable.

A small percentage of Consumer Loans in the United States are assigned to the Company in exchange for a single payment. Because the dealer-partner does not retain a financial interest in loans acquired in this manner, these loans are considered to be Purchased Loans (Purchased Loans) for accounting purposes.

Principal Business

A consumer who does not qualify for conventional automobile financing can purchase a used vehicle from a Credit Acceptance dealer-partner and finance the purchase through the Company. As payment for the vehicle, the dealer-partner receives the following:

(i) a down payment from the consumer;

(ii) a cash advance from the Company; and

(iii) after the advance has been recovered by the Company, the cash from payments made on the Consumer Loan, net of certain collection costs and the Company s servicing fee (dealer holdback).

The Company s servicing fee is equal to a fixed percentage (typically 20%) of each payment collected. In addition, the Company receives fees for other products and services provided in connection with Consumer Loans. Consumers and dealer-partners benefit as follows:

3

Consumers. The Company helps change the lives of consumers who do not qualify for conventional automobile financing by helping them obtain quality transportation and, equally important, providing an opportunity to establish or reestablish their credit through the timely repayment of their Consumer Loan.

Dealer-Partners. The Company s program increases dealer-partners profits in the following ways:

Enables dealer-partners to sell cars to consumers who may not be able to obtain financing without the Company s program. In addition, consumers often become repeat customers by financing future vehicle purchases either through the Company s program or, after they have successfully established or reestablished their credit, through conventional financing.

Allows dealer-partners to share in the profits not only from the sale of the vehicle, but also from its financing.

Enables dealer-partners to attract consumers by advertising guaranteed credit approval , where allowed by law. The consumers will often use other services of the dealer-partners and refer friends and relatives to them.

Enables dealer-partners to attract consumers who mistakenly assume they do not qualify for conventional financing.

Credit Acceptance derives its revenues from the following principal sources:

(i) Finance charges, which are comprised of: (a) servicing fees earned as a result of servicing Consumer Loans assigned to the Company by dealer-partners, (b) fees earned from the Company s third party ancillary product offerings, which primarily consist of service contract programs and (c) fees associated with the Dealer Loan including term extension fees;

(ii) license fees, which represent monthly fees charged to dealer-partners for access to the Company s patented Internet-based Credit Approval Processing System (CAPS);

(iii) other income, which primarily consists of: remarketing charges, fees charged to dealer-partners for enrolling in the Company s program, interest income on secured financing, and fees for marketing materials.

The following table sets forth the percent relationship to total revenue from continuing operations of each of these sources:

	For the Years Ended December 31,		
	2006	**2005**	**2004**
Percent of Total Revenue from Continuing Operations			
Finance charges	86.0%	87.6%	87.5%
License fees	6.2%	4.9%	3.4%
Other income	7.8%	7.5%	9.1%
Total revenue	100.0%	100.0%	100.0%

The Company s business is seasonal with peak Consumer Loan acceptances occurring during the first quarter of the year. However, this seasonality does not have a material impact on the Company s interim results.

The Company is organized into two primary business segments: United States and Other. The Other segment consists of a number of discontinued businesses including a United Kingdom automobile financing business, an automobile leasing business, a Canadian automobile financing business, and a business offering secured lines of credit and floorplan financing products. In early 2002, the Company stopped originating automobile leases and effective June 30, 2003 stopped accepting Consumer Loans originated in the United Kingdom and Canada. The Company sold the remaining Consumer Loan portfolio of its United Kingdom subsidiary on December 30, 2005. As of December 31,

2006, substantially all of the Company s capital was invested in the United States business segment. For information regarding the Company s reportable segments, see Note 10 to the consolidated financial statements, which is incorporated herein by reference.

Operations in the United States

Sales and Marketing. The Company s target market is a select group of the more than 70,000 independent and franchised automobile dealers in the United States. The marketing of the Company s program is intended to: (i) result in a network consisting of the highest quality dealer-partners who share the Company s commitment to changing lives and (ii) increase the value of the Company s program to the Company s dealer-partners. Dealer-partners pay an enrollment fee to join the Company s program. In return, the Company provides the dealer-partner with sales promotion kits, signs, training and the first month s access to CAPS. Dealer-partners have the option to pay a one-time enrollment fee of $9,850 to join the Company s program or to defer the fee. Dealer-partners choosing to defer the fee instead agree to allow the Company to keep 50% of the first accelerated dealer holdback payment. This payment, called Portfolio Profit Express, is paid to qualifying dealer-partners after 100 Consumer Loans have been originated and assigned to the Company.

Dealer-partner enrollments in the United States for each of the last five years are presented in the table below.

Year	Number of Dealer-Partner Enrollments
2002	143
2003	399
2004	534
2005	956
2006	1,172

A new dealer-partner is required to execute a dealer servicing agreement, which defines the legal relationship between the Company and the dealer-partner. The dealer servicing agreement assigns the responsibilities for administering, servicing and collecting the amounts due on Consumer Loans to the Company. The dealer servicing agreement provides that collections received by Credit Acceptance during a calendar month on Consumer Loans assigned by a dealer-partner are applied on a pool-by-pool basis as follows:

First, to reimburse Credit Acceptance for certain collection costs;

Second, to pay Credit Acceptance its servicing fee;

Third, to reduce the aggregate advance balance and to pay any other amounts due from the dealer-partner to the Company; and

Fourth, to the dealer-partner as payment for amounts contractually due under the dealer servicing agreement.

Under the typical dealer servicing agreement, a dealer-partner represents that it will only submit Consumer Loans to Credit Acceptance which satisfy criteria established by the Company, meet certain conditions with respect to the binding nature and the status of the security interest in the purchased vehicle, and comply with applicable state, federal and foreign laws and regulations. Dealer-partners receive a monthly statement from the Company, summarizing all activity on Consumer Loans assigned by such dealer-partner.

If the Company discovers a misrepresentation by the dealer-partner relating to a Consumer Loan assigned to the Company, the Company can demand that the Consumer Loan be repurchased for the current balance of the Consumer Loan less the amount of any unearned finance charge plus the applicable termination fee, which is generally $500. Upon receipt of such amount in full, the Company will reassign the Consumer Loan and its security interest in the financed vehicle to the dealer-partner. The dealer-partner can also opt to repurchase Consumer Loans at their own discretion.

The typical dealer servicing agreement may be terminated by the Company or by the dealer-partner upon written notice. The Company may terminate the dealer servicing agreement immediately in the case of an event of default by the dealer-partner. Events of default include, among other things:

(1) the dealer-partner s refusal to allow the Company to audit its records relating to the Consumer Loans assigned to the Company;

(2) the dealer-partner, without the Company s consent, is dissolved; merges or consolidates with an entity not affiliated with the dealer-partner; or sells a material part of its assets outside the course of its business to an entity not affiliated with the dealer-partner; or

(3) the appointment of a receiver for, or the bankruptcy or insolvency of, the dealer-partner.

While a dealer-partner can cease submitting Consumer Loans to the Company at any time without terminating the dealer servicing agreement, if the dealer-partner elects to terminate the dealer servicing agreement or in the event of a default, the dealer-partner must immediately pay the Company:

(i) any unreimbursed collection costs;

(ii) any unpaid advances and all amounts owed by the dealer-partner to the Company; and

(iii) a termination fee equal to 15% of the then outstanding amount of the Consumer Loans accepted by the Company.

Upon receipt of such amounts in full, the Company would reassign the Consumer Loans and its security interest in the financed vehicles to the dealer-partner. In the event of a termination by the Company (or any other termination if the Company and the dealer- partner agree), the Company may continue to service Consumer Loans accepted prior to termination in the normal course of business without charging a termination fee.

Consumer Loan Assignment. Once a dealer-partner has enrolled in the Company s program, the dealer-partner may begin submitting Consumer Loans to the Company for servicing, administration, and collection. A Consumer Loan occurs when a consumer enters into a contract with a dealer-partner that sets forth the terms of the agreement between the consumer and the dealer-partner for the payment of the purchase price of the automobile. The amount of the Consumer Loan consists of the total principal and interest that the consumer is required to pay over the term of the Consumer Loan. Virtually all of the Consumer Loans accepted by the Company in the United States are processed through CAPS. CAPS was offered beginning in January 2001, and allows dealer-partners to input a consumer s credit application and view the response from the Company via the Internet. CAPS allows dealer-partners to: (i) receive an approval from the Company much faster than with historical methods; and (ii) interact with the Company s credit scoring system to improve the structure of each transaction prior to delivery. All responses include the amount of the advance, as well as any stipulations required for funding. The amount of the advance is determined using a formula which considers a number of factors including the timing and amount of cash flows expected on the related Consumer Loan and the Company s target return on capital at the time the Consumer Loan is assigned. The estimated future cash flows are determined based upon a proprietary credit scoring system, which considers numerous variables, including the consumer s credit bureau report, data contained in the consumer s credit application, the structure of the proposed transaction, vehicle information and other factors, to calculate a composite credit score that corresponds to an expected collection rate. The Company s credit scoring system forecasts the collection rate based upon the historical performance of Consumer Loans in the Company s portfolio that share similar characteristics. The performance of the credit scoring system is evaluated monthly by comparing projected to actual Consumer Loan performance. Adjustments are made to the credit scoring system when necessary.

While a dealer-partner can assign any legally compliant Consumer Loan to the Company for servicing, administration and collection, the decision whether to pay an advance to the dealer-partner and the amount of any advance is made solely by the Company. The Company performs all significant functions relating to the processing of the Consumer Loan applications and bears certain costs of Consumer Loan acceptance, including the cost of assessing the adequacy of Consumer Loan documentation, compliance with underwriting guidelines and the cost of verifying employment, residence and other information submitted by the dealer-partner.

CAPS interfaces with the Company s Application and Contract System (ACS). Consumer Loan information included in CAPS is automatically entered into ACS through a download from CAPS. Additional Consumer Loan information is entered into ACS manually. ACS provides credit scoring capability as well as the ability to process Consumer Loan packages. ACS compares Consumer Loan data against information provided during the approval process and allows the funding analyst to check that all stipulations have been met prior to funding. Consumer Loan contracts are written on a contract form provided by the Company and the Consumer Loan transaction typically is not completed until the dealer-partner has received approval from the Company. The assignment of the Consumer Loan from the dealer-partner to the Company occurs after both the consumer and dealer-partner sign the contract and the original contract is received and approved by the Company. Although the dealer-partner is named in the Consumer Loan contract, the dealer-partner generally does not have legal ownership of the Consumer Loan for more than a moment and the Company, not the dealer-partner, is listed as lien holder on the vehicle title. The consumer s payment obligation is directly to the Company. Payments are generally made by the consumer directly to the Company. The consumer s failure to pay amounts due under the Consumer Loan will result in collection action by the Company.

The Company generally offers the dealer-partner a non-recourse advance against anticipated future collections on the Consumer Loan. Since typically the combination of the advance and the consumer s down payment provides the dealer-partner with a cash profit at the time of sale, the dealer-partner s risk in the Consumer Loan is limited. The Company cannot demand repayment from the dealer-partner of the advance except in the event the dealer-partner is in default of the dealer servicing agreement. Advances are made only after the Consumer Loan is approved, accepted by and assigned to the Company and all other stipulations required for funding have been satisfied.

Cash advanced to dealer-partners is automatically assigned to the originating dealer-partner s open pool of advances. The Company records the amount advanced to the dealer-partner as a Dealer Loan (Dealer Loan), which is classified within Loans receivable in the Company s consolidated balance sheets. At the dealer-partner s option, a pool containing at least 100 Consumer Loans can be closed and subsequent advances assigned to a new pool. All advances due from a dealer-partner are secured by the future collections on the dealer-partner s portfolio of Consumer Loans assigned to the Company. The Company perfects its security interest by taking possession of the Consumer Loans. Net collections on all related Consumer Loans within the pool, after payment of the Company s servicing fee and reimbursement of certain collection costs, are applied to reduce the aggregate advance balance owing against those Consumer Loans within the pool. Once the advance balance has been repaid, the dealer-partner is entitled to receive

future net collections from Consumer Loans within that pool, after payment of the Company s servicing fee and reimbursement of certain collection costs. If the collections on Consumer Loans from a dealer-partner s pool are not sufficient to repay the advance balance, the dealer-partner will not receive dealer holdback. Additionally, for dealer-partners with more than one pool, the pools are cross-collateralized so the performance of other pools is considered in determining eligibility for dealer holdback.

Dealer-partners have an opportunity to receive a portion of the dealer holdback on an accelerated basis at the time a pool of 100 or more Consumer Loans is closed. The eligibility to receive accelerated dealer holdback and the amount paid to the dealer-partner is calculated using a formula that considers the collection rate and the advance balance on the closed pool.

The Company s business model allows it to share the risk and reward of collecting on the Consumer Loans with the dealer-partners. Such sharing is intended to motivate the dealer-partner to assign better quality Consumer Loans, follow the Company s underwriting guidelines, and provide appropriate service and support to the consumer after the sale. The Company believes this arrangement aligns the interests of the Company, the dealer-partner and the consumer. The Company measures various criteria for each dealer-partner against other dealer-partners in their area as well as the top performing dealer-partners. Sales representatives present the analysis to the dealer-partner as needed to develop an action plan with the dealer-partner to improve the dealer-partner s overall success with the Company s program.

Information on the Company s Consumer Loans is presented in the following table:

	For the Years Ended December 31,				
Average Consumer Loan Data	**2006**	**2005**	**2004**	**2003**	**2002**
Average size of Consumer Loan accepted	$12,729	$11,980	$12,634	$12,143	$11,202
Percentage growth in average size of Consumer Loan	6.3%	(5.2)%	4.0%	8.4%	7.7%
Average initial maturity (in months)	37	34	37	37	36

Servicing and Collections. The Company s collectors are organized into teams. The Company s first payment missed team services Consumer Loans of consumers who have failed to make one of their first three payments on time. A collection call is generally placed to these consumers within one day after the payment is due. Once a consumer has made their first three payments, the consumers are segmented by delinquency and phone contact profile. The daily contact strategy matches delinquency and contact segments with appropriate collector skill sets with the goal of maximizing cash collections. The Company has an incentive system to encourage collectors to collect the full amount due and eliminate the delinquency on Consumer Loans assigned to their team. Collectors may recommend repossession of the vehicle based on a variety of factors including the amount of the delinquency and the estimated value of the vehicle. These recommendations are typically reviewed by a collection team supervisor.

When a Consumer Loan is approved for repossession, the account is transferred to the Company s repossession team. Repossession personnel continue to service the Consumer Loan as it is being assigned to a third party repossession contractor, who works on a contingency fee basis. Once a vehicle has been repossessed, the consumer can negotiate a redemption with the Company, whereby the vehicle is returned to the consumer in exchange for paying off the Consumer Loan balance, or where appropriate or if required by law, the vehicle is returned to the consumer and the Consumer Loan reinstated, in exchange for reducing or eliminating the past due balance. If the redemption process is not successful, the vehicle is typically sold at a wholesale automobile auction. Prior to sale, the vehicle is usually inspected by the Company s remarketing representatives who authorize repair and reconditioning work in order to maximize the net sale proceeds at auction.

If the vehicle sale proceeds are not sufficient to satisfy the balance owing on the Consumer Loan, the Consumer Loan is serviced by either: (i) the Company s senior collection team, in the event that the consumer is willing to make payments on the deficiency balance; or (ii) where permitted by law, the Company s legal team, if it is believed that legal action is required to reduce the deficiency balance owing on the Consumer Loan. The Company s legal team assigns Consumer Loans to third party collection attorneys who file a claim and upon obtaining a judgment, garnish

wages or other assets ; or (iii) to a third party collection company.

Collectors rely on two systems to service accounts, the Collection System (CS) and the Loan Servicing System (LSS). The CS and LSS are connected through a batch interface. The present CS has been in service since June 2002. The CS interfaces with a predictive dialer and records all activity on a Consumer Loan, including details of past phone conversations with the consumer, collection letters sent, promises to pay, broken promises, repossession orders and collection attorney activity. The LSS maintains a record of all transactions relating to Consumer Loans assigned after July 1990 and is a primary source of management reporting including data utilized to:

(i) evaluate the Company s proprietary credit scoring system;

(ii) forecast future collections;

(iii) establish the amount of revenue recognized by the Company; and

(iv) analyze the profitability of the Company s program.

During the third quarter of 2005, the Company began an initiative to outsource a portion of its collection function to a company in India. In the second quarter of 2006, the Company entered into another outsourcing arrangement with a company in Costa Rica. These outsourced collectors service accounts using the Collection System and typically work on accounts that are less than sixty days past due. The Company expects the outsourcing to minimize the geographic risk of having two collection centers in the United States, provide additional flexibility and to reduce costs.

Service Contracts and Insurance Products

The Company provides dealer-partners the ability to offer vehicle service contracts to consumers. Under this program, the sales price of the service contract is added to the amount due under the Consumer Loan. The cost of the service contract, plus a commission earned by the dealer-partner on the sale of the service contract is added to the advance balance. A portion of the amount added to the advance balance is retained by the Company as a fee. Third party vehicle service contract administrators (TPAs) bear all of the risk of loss on claims. During 2004, the Company entered into agreements with two TPAs through which the Company is eligible to receive underwriting profits from the TPAs based on the level of future claims paid. The Company will be eligible in 2007 to receive profits related to 2004. Funds paid by the Company to the TPA to pay future claims are held in trusts. The assets and liabilities of the trusts have been consolidated on the Company s balance sheet in accordance with Financial Accounting Standards Board (FASB) Interpretation No. 46, Consolidation of Variable Interest Entities (FIN 46). As of December 31, 2006, the trusts had $18.2 million in assets available to pay claims and a related claims reserve of $17.7 million. For additional information regarding the two TPAs, see Note 1 to the consolidated financial statements, which is incorporated herein by reference.

The Company maintains relationships with certain insurance carriers which provide dealer-partners the ability to offer consumers credit life and disability insurance. Should the consumer elect to purchase this insurance, the premium on the insurance policy is added to the amount due under the Consumer Loan and to the advance balance. The Company is not involved in the actual sale of the insurance; however, the insurance carrier cedes the premiums, less a fee, to a wholly-owned subsidiary of the Company, which reinsures the coverage under the policy. As a result, the Company, through its subsidiary, bears the risk of loss, and earns revenues from premiums ceded and the investment of such funds. The Company s reserve for insurance claims was $0.1 million and $0.2 million at December 31, 2006 and 2005, respectively. The Company ceased offering this product in November 2003.

During the first quarter of 2005, the Company began offering Guaranteed Asset Protection (GAP) debt cancellation terms in its contracts. GAP provides the consumer protection by paying the difference between the loan balance and the consumer s insurance coverage limit in the event the vehicle is totaled or stolen. The Company receives a fee for every GAP product sold by its dealer-partners. The cost of GAP, the Company s fee, plus a commission earned by the dealer-partner on the sale of GAP, is added to the advance balance.

Businesses in Liquidation

Effective June 30, 2003, the Company decided to stop originating Consumer Loans in the United Kingdom. The Company sold the remaining Consumer Loan portfolio of its United Kingdom subsidiary on December 30, 2005. The selling price was approximately $4.3 million resulting in a pre-tax gain of approximately $3.0 million.

Effective June 30, 2003, the Company decided to stop accepting Consumer Loans in Canada. Prior to this decision, the Company accepted and serviced Consumer Loans in Canada on approximately the same basis as in the United States.

In January 2002, the Company decided to exit the automobile leasing business. Prior to this decision, the Company assumed ownership of automobile leases from dealer-partners for an amount based on the value of the vehicle as determined by an industry guidebook, assumed ownership of the related vehicle from the dealer-partner and received

title to the vehicle. This program differed from the Company s principal business in that the Company assumed ownership of the vehicles and assumed no liability to the dealer-partner for dealer holdback payments.

The Company offered line of credit arrangements to certain dealers who were not participating in the Company s core program. These lines of credit are secured primarily by loans, originated and serviced by the dealer, with additional security provided by the personal guarantee of the dealership s owner. The effective interest rate on these loans varies based upon the amount loaned to the dealer and the percentage of collections on the loan portfolio required to be remitted to the Company. During the third quarter of 2001, the Company discontinued offering this program to new dealers and is in the process of reducing the amount of capital invested in this business.

Credit Loss Policy

For information regarding the Company s accounting policy for the allowance for credit losses, see Note 1 to the consolidated financial statements, which is incorporated herein by reference.

Competition

The market for consumers who do not qualify for conventional automobile financing is large and highly competitive. The Company s largest competition comes from buy here, pay here dealerships where the dealer finances the consumer s purchase and services the Consumer Loan themselves. The market is also currently served by banks, captive finance affiliates of automobile manufacturers, credit unions and independent finance companies both publicly and privately owned. Many of these companies are much larger and have greater resources than the Company. These companies typically target higher credit tier customers within the Company s market. In seeking to establish the Company as one of the principal financing sources of its dealer-partners, the Company competes predominantly on the basis of a high level of dealer-partner service and strong dealer-partner relationships, and by offering guaranteed credit approval for consumers. While the Company is aware of only a few companies that offer guaranteed credit approval, there is the potential that significant direct competition could emerge and that the Company may be unable to compete successfully.

Customer and Geographic Concentrations

No single dealer-partner accounted for more than 10% of total revenues during any of the last three years. Additionally, no single dealer-partner s Dealer Loan balance accounted for more than 10% of total Dealer Loans as of December 31, 2006 or as of December 31, 2005. The following table provides information regarding the five states that are responsible for the largest dollar amount of Consumer Loans accepted in the United States during 2006:

	Consumer Loans Accepted		Active Dealer-Partners (1)	
(Dollars in thousands)	**Amount**	**% of Total**	**Number**	**% of Total**
Texas	$ 99,398	8.3%	138	6.2%
Alabama	90,836	7.6	73	3.3
Michigan	88,792	7.4	161	7.2
Mississippi	70,621	5.9	58	2.6
New York	68,197	5.7	145	6.5
All other states	785,187	65.1	1,657	74.2
Total	$ 1,203,031	100.0%	2,232	100.0%

(1) Active dealer-partners are dealer-partners who submitted at least one Consumer Loan during the year.

The following table provides information regarding the five states that are responsible for the largest dollar amount of Consumer Loans accepted in the United States during 2005:

	Consumer Loans Accepted	Active Dealer-Partners (1)
(Dollars in thousands)	**Amount**	**Number**

		% of Total		% of Total
Michigan	$ 84,338	8.4%	161	9.1%
Alabama	67,508	6.7	59	3.3
Mississippi	67,252	6.7	56	3.2
New York	59,461	5.9	108	6.1
Texas	58,678	5.9	109	6.2
All other states	663,882	66.4	1,273	72.1
Total	$ 1,001,119	100.0%	1,766	100.0%

(1) Active dealer-partners are dealer-partners who submitted at least one Consumer Loan during the year.

While not considered to be a concentration, the Company s transactions with related parties are significant. For information regarding the Company s transactions with related parties, see Note 7 to the consolidated financial statements, which is incorporated herein by reference.

Table of Contents

Geographic Financial Information

The following table sets forth, for each of the last three years for the Company s domestic and foreign operations, the amount of revenues and long-lived assets:

(In thousands)	As of and for the Years Ended December 31, 2006	2005	2004
Revenues from Continuing Operations			
United States	$ 219,077	$ 200,641	$ 171,111
Other foreign	255	627	960
Total revenues from continuing operations	$ 219,332	$ 201,268	$ 172,071
Long-lived assets			
United States	$ 16,203	$ 17,992	$ 19,474
Other foreign			232
Total long-lived assets	$ 16,203	$ 17,992	$ 19,706

Regulation

The Company s businesses are subject to various state, federal and foreign laws and regulations, which:

(i) require licensing and qualification,

(ii) regulate interest rates, fees and other charges,

(iii) require specified disclosures to consumers,

(iv) govern the sale and terms of ancillary products; and

(v) define the Company s rights to collect Consumer Loans and repossess and sell collateral.

Failure to comply with, or an adverse change in, these laws or regulations could have a material adverse effect on the Company by, among other things, limiting the states or countries in which the Company may operate, restricting the Company s ability to realize the value of the collateral securing the Consumer Loans, or resulting in potential liability related to the servicing of Consumer Loans accepted from dealer-partners. In addition, governmental regulations depleting the supply of used vehicles, such as environmental protection regulations governing emissions or fuel consumption, could have a material adverse effect on the Company. The Company is not aware of any such legislation currently pending that could have a material adverse effect on the Company.

The sale of insurance products in connection with Consumer Loans assigned to the Company by dealer-partners is also subject to state laws and regulations. However, as the Company does not deal directly with consumers in the sale of insurance products, it does not believe that such laws and regulations significantly affect its business. Nevertheless, there can be no assurance that insurance regulatory authorities in the jurisdictions in which such products are offered by dealer-partners will not seek to regulate the Company or restrict the operation of the Company s business in such jurisdictions. Any such action could materially adversely affect the income received from such products. The Company s credit life and disability reinsurance and property and casualty insurance subsidiaries are licensed and subject to regulation in the Turks and Caicos Islands.

The Company believes that it maintains all material licenses and permits required for its current operations and is in substantial compliance with all applicable laws and regulations. The Company s dealer servicing agreement with dealer-partners provides that the dealer-partner shall indemnify the Company with respect to any loss or expense the Company incurs as a result of the dealer-partner s failure to comply with applicable laws and regulations.

10

Table of Contents

Team Members

As of December 31, 2006, the Company had 788 full and part-time team members. The Company s team members have no union affiliations and the Company believes its relationship with its team members is good. The table below presents team members by department:

Department	Number of Team Members December 31, 2006	2005
Collection and Servicing	423	474
Loan Origination and Processing	100	52
Sales and Marketing	103	92
Finance and Accounting	38	37
Information Systems	63	67
Management and Support	61	55
Total	788	777

ITEM 1A. RISK FACTORS

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

The ability to accurately forecast Consumer Loan performance is critical to the Company s success. At the time of Consumer Loan acceptance, the Company forecasts future expected cash flows from the Consumer Loan. Based on these forecasts, the Company makes an advance to the related dealer-partner at a level designed to achieve an acceptable return on capital. If Consumer Loan performance equals or exceeds original expectations, it is likely the target return on capital will be achieved. However, actual cash flows from any individual Dealer Loan are often different than cash flows estimated at Dealer Loan inception. If such difference is favorable, the difference is recognized into income over the remaining life of the Dealer Loan through a yield adjustment. If such difference is unfavorable, an allowance for credit losses is established and a corresponding provision for credit losses is recorded as a current period expense. Because there are differences between estimated cash flows at inception and actual cash flows, an allowance is required for a significant portion of the Company s Dealer Loan portfolio. There can be no assurance that estimates will be accurate or that Consumer Loan performance will be as expected. If the Company produces disappointing operating results, it will likely be because future Consumer Loan performance was overestimated. In the event that the Company underestimates the default risk or under-prices products, the financial position, liquidity and results of operations will be adversely affected, possibly to a material degree.

Due to increased competition from traditional financing sources and non-traditional lenders, the Company may not be able to compete successfully.

The automobile finance market is highly fragmented and is served by a variety of companies. The Company s largest competition comes from buy here, pay here dealerships where the dealer finances the consumer s purchase and services the Consumer Loan themselves. The market is also currently served by banks, captive finance affiliates of automobile manufacturers, credit unions and independent finance companies both publicly and privately owned. Many of these companies are much larger and have greater financial resources than are available to the Company, and many have long standing relationships with automobile dealerships. Providers of automobile financing have traditionally competed based on the interest rate charged, the quality of credit accepted, the flexibility of loan terms offered and the quality of service provided to dealers and consumers. In seeking to establish the Company as one of the principal financing sources of its dealer-partners, the Company competes predominately on the basis of a high level of dealer service and strong dealer relationships, and by offering guaranteed credit approval for consumers. While the Company is aware of only a few companies that offer guaranteed credit approval, there is potential that significant direct competition could emerge and that the Company may be unable to compete successfully.

The Company s ability to maintain and grow the business is dependent on the ability to continue to access funding sources and obtain capital on favorable terms.

The Company has two revolving credit facilities: a $135.0 million line of credit which matures on June 20, 2008 with a commercial bank syndicate and a $325.0 million warehouse facility which matures on February 13, 2008 with institutional investors. In addition, the Company utilizes Rule 144A asset backed secured borrowings with qualified institutional investors and has access to a residual credit facility. There can be no assurance that new or additional financing can be obtained, or that it will be available on acceptable terms. If its various financing alternatives were to become limited or unavailable, the Company would have to limit business activity, and operations could be materially adversely affected.

The Company may not be able to generate sufficient cash flow to service its outstanding debt and fund operations.

The Company currently has substantial outstanding indebtedness and its credit facilities allow the Company to incur significant amounts of additional debt. The ability to make payment of principal or interest on indebtedness will depend in part on the Company s future operating performance, which to a certain extent is subject to economic, financial, competitive and other factors beyond the Company s control. If the Company is unable to generate sufficient cash flow in the future to service its debt, it may be required to refinance all or a portion of its existing debt or to obtain additional financing. There can be no assurance that any such refinancing will be possible or that any additional financing can be obtained on sustainable terms.

12

The substantial regulation to which the Company is subject limits the business and could result in potential liability.

The Company s business is subject to various laws and regulations which require licensing and qualification; limit interest rates, fees and other charges associated with the Consumer Loans assigned to the Company; require specified disclosures by dealer-partners to consumers; govern the sale and terms of ancillary products; and define the rights to repossess and sell collateral. Failure to comply with, or an adverse change in, these laws or regulations could have a material adverse effect on the Company by, among other things, limiting the jurisdictions in which the Company may operate, restricting the ability to realize the value of the collateral securing the Consumer Loans, making it more costly or burdensome to do business, or resulting in potential liability. In addition, governmental regulations which would deplete the supply of used vehicles, such as environmental protection regulations governing emissions or fuel consumption, could have a material adverse effect on the Company.

The sale of insurance products in connection with Consumer Loans assigned to the Company by dealer-partners is also subject to state laws and regulations. As the holder of the Consumer Loans that contain these products, some of these state laws and regulations may apply to the Company s servicing and collection of the Consumer Loans. Although the Company does not believe that such laws and regulations significantly affect its business because it does not deal directly with consumers in the sale of insurance products, there can be no assurance that insurance regulatory authorities in the jurisdictions in which such products are offered by dealer-partners will not seek to regulate or restrict the operation of the business in such jurisdictions. Any such action could materially adversely affect the income received from such products.

Adverse changes in economic conditions, or in the automobile or finance industries or the non-prime consumer market, could adversely affect the Company s financial position, liquidity and results of operations and its ability to enter into future financing transactions.

The Company is subject to general economic conditions which are beyond its control. During periods of economic slowdown or recession, delinquencies, defaults, repossessions and losses generally increase. These periods also may be accompanied by decreased consumer demand for automobiles and declining values of automobiles securing outstanding Consumer Loans, which weakens collateral coverage and increases the amount of a loss in the event of default. Significant increases in the inventory of used automobiles during periods of economic recession may also depress the prices at which repossessed automobiles may be sold or delay the timing of these sales. Because the business is focused on consumers who do not qualify for conventional automobile financing, the actual rates of delinquencies, defaults, repossessions and losses on these Consumer Loans could be higher than that of those experienced in the general automobile finance industry, and could be more dramatically affected by a general economic downturn. In addition, during an economic slowdown or recession, the Company s servicing costs may increase without a corresponding increase in service fee income. Any sustained period of increased delinquencies, defaults, repossessions or losses or increased servicing costs could also materially adversely affect the Company s financial position, liquidity and results of operations and its ability to enter into future financing transactions.

Litigation the Company is involved in from time to time may adversely affect its financial condition, results of operations and cash flows.

As a result of the consumer-oriented nature of the industry in which the Company operates and uncertainties with respect to the application of various laws and regulations in some circumstances, the Company is subject to various consumer claims and litigation seeking damages and statutory penalties, based upon, among other things, usury, disclosure inaccuracies, wrongful repossession, violations of bankruptcy stay provisions, certificate of title disputes, fraud and breach of contract. Some litigation against the Company could take the form of class action complaints by consumers. As the assignee of Consumer Loans originated by dealer-partners, it may also be named as a co-defendant in lawsuits filed by consumers principally against dealer-partners. The damages and penalties claimed by consumers in these types of matters can be substantial. The relief requested by the plaintiffs varies but includes requests for compensatory, statutory and punitive damages. A significant judgment against the Company in connection with any litigation could have a material adverse effect on the Company s financial condition and results of operations.

Table of Contents

The Company is dependent on its senior management and the loss of any of these individuals or an inability to hire additional personnel could adversely affect its ability to operate profitably.

The Company s senior management average over 8 years of experience with the Company. The Company s success is dependent upon the management and the leadership skills of these managers. In addition, competition from other companies to hire the Company s personnel possessing the necessary skills and experience required could contribute to an increase in employee turnover. The loss of any of these individuals or an inability to attract and retain additional qualified personnel could adversely affect the Company. There can be no assurance that the Company will be able to retain its existing senior management personnel or attract additional qualified personnel.

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

Natural disasters, acts of war, terrorist attacks and the escalation of military activity in response to such attacks or otherwise may have negative and significant effects, such as imposition of increased security measures, changes in applicable laws, market disruptions and job losses. Such events may have an adverse effect on the economy in general. Moreover, the potential for future terrorist attacks and the national and international responses to such threats could affect the business in ways that cannot be predicted. The effect of any of these events or threats could have an adverse effect on the Company s business, financial condition and results of operations.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

United States and Other

The Company s headquarters are located at 25505 West Twelve Mile Road, Southfield, Michigan 48034. The Company purchased the office building in 1993 and has a mortgage loan from a commercial bank that is secured by a first mortgage lien on the property. The office building includes approximately 118,000 square feet of space on five floors. The Company occupies approximately 98,000 square feet of the building, with most of the remainder of the building leased to various tenants.

The Company leases approximately 20,000 square feet of office space in Henderson, Nevada. The lease expires in October 2009.

United Kingdom

The Company leases approximately 10,000 square feet of office space in an office building in Worthing, West Sussex, in the United Kingdom. As of December 31, 2006, the Company did not occupy any space within the building under the lease expiring in September 2007.

ITEM 3. LEGAL PROCEEDINGS

In the normal course of business and as a result of the consumer-oriented nature of the industry in which the Company operates, industry participants are frequently subject to various consumer claims and litigation seeking damages and statutory penalties. The claims allege, among other theories of liability, violations of state, federal and foreign truth-in-lending, credit availability, credit reporting, consumer protection, warranty, debt collection, insurance and other consumer-oriented laws and regulations, including claims seeking damages for physical and mental damages relating to the Company s repossession and sale of the consumer s vehicle and other debt collection activities. As the Company accepts assignments of Consumer Loans originated by dealer-partners, it may also be named as a co-defendant in lawsuits filed by consumers principally against dealer-partners. Many of these cases are filed as purported class actions and seek damages in large dollar amounts. An adverse ultimate disposition in any such action could have a material adverse impact on the Company s financial position, liquidity and results of operations.

For a description of material pending litigation to which the Company is a party, see Note 12 to the consolidated financial statements, which is incorporated herein by reference.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of the shareholders during the fourth quarter of 2006.

Table of Contents

PART II

ITEM 5. MARKET FOR REGISTRANT S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Stock Price

From January 1, 2005 through July 18, 2005 and from April 26, 2006 through December 31, 2006, the Company s common stock was traded on The Nasdaq Global Market® (Nasdaq) under the symbol CACC. From July 19, 2005 until April 25, 2006, the Company s common stock was delisted from the Nasdaq and was traded on the Pink Sheets Electronic Quotation Service (Pink Sheets) under the symbol CACC until it was relisted on the Nasdaq with trading in its common shares beginning on April 26, 2006. The following table sets forth the high and low sale prices as reported by the Nasdaq for the common stock for each quarter during 2005 and 2006 that the common stock was traded on the Nasdaq and the high and low bid prices for the common stock for each quarter during 2005 and 2006 that the common stock was traded on the Pink Sheets. Such bid information reflects inter-dealer prices, without retail mark-up, mark-down or commission and may not necessarily represent actual transactions.

	2006		2005	
Quarter Ended	**High**	**Low**	**High**	**Low**
March 31	$25.00	$15.89	$26.46	$19.16
June 30	30.55	23.05	20.09	12.90
September 30	30.70	24.53	16.25	12.08
December 31	34.59	30.10	17.90	14.50

As of February 16, 2007, the number of beneficial holders and shareholders of record of the common stock was 1,938 based upon securities position listings furnished to the Company.

Dividends

The Company has not paid any cash dividends during the periods presented. The Company s credit agreements contain financial covenants pertaining to the Company s ratio of liabilities to tangible net worth and amount of tangible net worth, which may indirectly limit the payment of dividends on common stock.

Table of Contents

Stock Performance Graph

The following graph compares the percentage change in the cumulative total shareholder return on the Company s common stock during the period beginning January 1, 2002 and ending on December 31, 2006 with the cumulative total return on the Nasdaq Market Index and a peer group index based upon approximately 100 companies included in the Dow Jones US General Financial Index. The comparison assumes that $100 was invested on January 1, 2002 in the Company s common stock and in the foregoing indices and assumes the reinvestment of dividends.

COMPARE 5 - YEAR CUMULATIVE TOTAL RETURN
AMONG CREDIT ACCEPTANCE CORP.,
NASADAQ MARKET INDEX AND DJ US GENERAL FINANCE INDEX

ASSUMES $100 INVESTED ON
JAN. 1, 2002 ASSUMES DIVIDENDS
REINVESTED FISCAL YEAR
ENDING DEC. 31, 2006

Equity Compensation Plans

The Company s Incentive Compensation Plan (the Incentive Plan), which was approved by shareholders on May 13, 2004, provides for the granting of restricted stock, restricted stock units, stock options, and performance awards to employees, officers, and directors. The Company also has two stock option plans pursuant to which it has granted stock options with time or performance-based vesting requirements to employees, officers, and directors. The Company s 1992 Stock Option Plan (the 1992 Plan) was approved by shareholders in 1992 prior to the Company s initial public offering and was terminated as to future grants on May 13, 2004, when shareholders approved the Incentive Plan. The Company s Director Stock Option Plan (the Director Plan) was approved by shareholders in 2002 and was terminated as to future grants on May 13, 2004, with shareholder approval of the Incentive Plan. The following table sets forth, with respect to each of the equity compensation plans, (i) the number of shares of common stock to be issued upon the exercise of outstanding options, (ii) the weighted average exercise price of outstanding options, and (iii) the number of shares remaining available for future issuance, as of December 31, 2006:

Plan Category	Number of shares to be issued upon exercise of outstanding options	Weighted-average exercise price of outstanding options	Number of shares remaining available for future issuance under equity compensation plans (a)
Equity compensation plans approved by shareholders:			
1992 Plan	1,653,041	$ 7.68	
Director Plan	100,000	17.25	
Incentive Plan			853,972
Total	1,753,041	$ 8.23	853,972

(a) For additional information regarding the Company s stock compensation plans, see Note 9 to the consolidated financial statements, which is incorporated herein by reference.

Stock Repurchases

The Company s board of directors approved a stock repurchase program which authorizes the Company to purchase common shares in the open market or in privately negotiated transactions at price levels the Company deems attractive. As of December 31, 2006, the Company has repurchased approximately 7.5 million shares under the stock

repurchase program at a cost of $85.3 million. As of December 31, 2006 the Company had approval from the board of directors to repurchase up to $8.6 million in common stock.

The following table summarizes the Company s stock repurchases for the three months ended December 31, 2006:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Dollar Value that May Yet Be Used to Purchase Shares Under the Plans or Programs
October 1 through October 31, 2006		$		$ 22,529,186
November 1 through November 30, 2006	441,182	31.50	441,182	8,631,953
December 1 through December 31, 2006				8,631,953
	441,182	$ 31.16	441,182	

17

Table of Contents

Modified Dutch Tender Offers

In addition to the stock repurchase program, the Company has repurchased 12.5 million shares of its common stock at a cost of $304.4 million through four modified Dutch auction tender offers completed since the beginning of 2004.

Commencement Date	Expiration Date	Number of Shares Tendered	Number of Shares Repurchased	Purchase Price per Share	Total Cost (in thousands)
November 26, 2003	January 6, 2004	2,201,744	2,201,744	$ 17.00	$ 37,430
August 11, 2004	September 9, 2004	2,673,073	2,673,073	20.00	53,461
February 10, 2006	March 13, 2006	4,129,735	4,129,735	25.00	103,243
August 28, 2006	September 26, 2006	20,552,028	3,500,000	31.50	110,250
			12,504,552		$304,384

Table of Contents

ITEM 6. SELECTED FINANCIAL DATA

The selected income statement and balance sheet data presented below are derived from the Company s audited consolidated financial statements and should be read in conjunction with the Company s consolidated financial statements for the years ended December 31, 2006, 2005, and 2004, and notes thereto and Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations , included elsewhere in this Annual Report. Certain amounts for prior periods have been reclassified to conform to the current presentation.

	(Dollars in Thousands, Except Per Share Data)				
	2006	**2005**	**2004**	**2003**	**2002**
Income Statement Data:					
Revenue	$ 219,332	$ 201,268	$ 172,071	$ 141,042	$ 138,070
Costs and expenses (A)	128,686	94,724	87,395	79,681	95,341
Operating income	90,646	106,544	84,676	61,361	42,729
Foreign currency (loss) gain	(6)	1,812	1,650	(2,767)	(3)
Income from continuing operations before provision for income taxes	90,640	108,356	86,326	58,594	42,726
Provision for income taxes	31,793	40,159	30,073	27,369	18,747
Income from continuing operations	58,847	68,197	56,253	31,225	23,979
(Loss) gain from operations of discontinued United Kingdom segment (B)	(297)	6,194	1,556	(7,047)	8,630
(Benefit) provision for income taxes	(90)	1,790	484	(491)	2,835
(Loss) gain from discontinued operations	(207)	4,404	1,072	(6,556)	5,795
Net income	$ 58,640	$ 72,601	$ 57,325	$ 24,669	$ 29,774
Net income per common share:					
Basic	$ 1.78	$ 1.96	$ 1.48	$ 0.58	$ 0.70
Diluted	$ 1.66	$ 1.85	$ 1.40	$ 0.57	$ 0.69
Income from continuing operations per common share:					

Basic	$	1.78	$	1.84	$	1.46	$	0.74	$	0.57
Diluted	$	1.67	$	1.74	$	1.37	$	0.72	$	0.55
(Loss) gain from discontinued operations per common share:										
Basic	$	(0.01)	$	0.12	$	0.03	$	(0.16)	$	0.14
Diluted	$	(0.01)	$	0.11	$	0.03	$	(0.15)	$	0.13
Weighted average shares outstanding:										
Basic		33,035,693		36,991,136		38,617,787		42,195,340		42,438,292
Diluted		35,283,478		39,207,680		41,017,205		43,409,007		43,362,741
Balance Sheet Data:										
Loans receivable, net	$	625,780	$	563,528	$	526,011	$	476,128	$	456,908
All other assets		99,433		55,866		65,302		68,720		68,251
Total assets	$	725,213	$	619,394	$	591,313	$	544,848	$	525,159
Total debt	$	392,175	$	146,905	$	193,547	$	106,447	$	109,663
Dealer reserve payable, net						15,675		35,198		47,262
Other liabilities		122,691		99,463		81,201		59,908		52,222
Total liabilities		514,866		246,368		290,423		201,553		209,147
Shareholders equity (C)		210,347		373,026		300,890		343,295		316,012
Total liabilities and shareholders equity	$	725,213	$	619,394	$	591,313	$	544,848	$	525,159

(A) Includes $11.2 million of additional legal expenses recorded in 2006 related to an increase in the Company s estimated loss related to a pending class action lawsuit in the state of Missouri.

(B)

Includes gain on sale of United Kingdom loan portfolio of $3.0 million recognized in 2005 and impairment expenses of $10.5 million recognized in 2003 following the decision to liquidate the United Kingdom operation.

(C) No dividends were paid during the periods presented.

ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Executive Summary

Since 1972, Credit Acceptance has provided auto loans to consumers, regardless of their credit history. The Company s product is offered through a nationwide network of automobile dealers who benefit from sales of vehicles to consumers who otherwise could not obtain financing; from repeat and referral sales generated by these same customers; and from sales to customers responding to advertisements for the Company s product, but who actually end up qualifying for traditional financing.

The Company is an indirect lender from a legal perspective, meaning the Consumer Loan is originated by the dealer-partner and immediately assigned to the Company. Typically, the compensation paid to the dealer-partner in exchange for the Consumer Loan is paid in two parts. A portion of the compensation is paid at the time of origination, and a portion is paid over time. The amount paid at the time of origination is called an advance; the portion paid over time is based on the performance of the loan and is called dealer holdback.

For accounting purposes, the transactions described above are not considered to be loans to consumers. Instead, the Company s accounting reflects that of a lender to the dealer-partner. This classification for accounting purposes is primarily a result of (i) the dealer-partner s financial interest in the Consumer Loan and (ii) certain elements of the Company s legal relationship with the dealer-partner. The cash amount advanced to the dealer-partner is recorded as an asset on the Company s balance sheet. The aggregate amount of all advances to an individual dealer-partner, plus accrued income, less repayments comprises the amount recorded in Loans receivable.

A small percentage of Consumer Loans in the United States are assigned to the Company in exchange for a single payment. Because the dealer-partner does not retain a financial interest in loans acquired in this manner, these loans are considered to be Purchased Loans (Purchased Loans) for accounting purposes.

The Company believes it has been successful in improving the profitability of its business in recent years primarily as a result of maintaining an adequate spread between the forecasted collection rate and the advance rate and increasing revenue from license fees and ancillary products. Dealer Loan dollar volume increased 15.4% in 2006 compared to 2005 primarily due to an increase in the number of active dealer-partners and an increase in the average transaction size. Since the Company believes it is one of only a few financial services companies serving the Company s target market, the Company believes that it has an opportunity to grow its business profitably in the future.

Critical success factors for the Company include access to capital and the ability to accurately forecast Consumer Loan performance. The Company s strategy for accessing the capital required to grow its business is to: (i) maintain consistent financial performance, (ii) maintain modest financial leverage, and (iii) maintain multiple funding sources. The Company s funded debt to equity ratio is 1.9 to 1.0 at December 31, 2006. The Company currently funds its business through four primary sources of financing: (i) a revolving line of credit with a commercial bank syndicate; (ii) a revolving secured warehouse facility with institutional investors; (iii) 144A asset backed securitizations with qualified institutional investors; and (iv) a residual credit facility.

The ability to accurately forecast Consumer Loan performance is critical to the Company. At the time of Consumer Loan acceptance, the Company forecasts future expected cash flows from the Consumer Loan. Based on these forecasts, an advance is made to the related dealer-partner at a level designated to achieve an acceptable return on capital. If Consumer Loan performance equals or exceeds the Company s original expectation, it is likely the Company s target return on capital will be achieved.

Consumer Loan Performance in the United States

Although the majority of loan originations are recorded in the Company s financial statements as Dealer Loans, each transaction starts with a loan from the dealer-partner to the individual purchasing the vehicle. Since the cash flows available to repay the Dealer Loans are generated, in most cases, from the underlying Consumer Loan, the performance of the Consumer Loans is critical to the Company s financial results. The following table presents forecasted Consumer Loan collection rates, advance rates, the spread (the forecasted collection rate less the advance rate), and the percentage of the forecasted collections that have been realized as of December 31, 2006 for the United States business segment. Payments of dealer holdback and accelerated payments of dealer holdback are not included in the analysis of the initial advance paid to the dealer-partner. All amounts are presented as a percentage of the initial balance of the Consumer Loan (principal + interest).

	As of December 31, 2006			
Year of Origination	**Forecasted Collection %**	**Advance %**	**Spread %**	**% of Forecast Realized**
1996	55.1%	46.9%	8.2%	100.0%
1997	58.4%	47.8%	10.6%	99.8%
1998	67.5%	46.0%	21.5%	99.2%
1999	72.4%	48.7%	23.7%	98.4%
2000	73.0%	47.9%	25.1%	97.6%
2001	67.7%	46.0%	21.7%	97.2%
2002	70.7%	42.2%	28.5%	96.9%
2003	74.2%	43.4%	30.8%	95.0%
2004	73.9%	44.0%	29.9%	83.6%
2005	73.8%	46.9%	26.9%	63.1%
2006	70.5%	46.6%	23.9%	22.0%

The following table compares the Company s forecast of Consumer Loan collection rates as of December 31, 2006 with the forecast as of December 31, 2005:

Year of Origination	**December 31, 2006 Forecasted Collection %**	**December 31, 2005 Forecasted Collection %**	**Variance**
1996	55.1%	55.0%	0.1%
1997	58.4%	58.3%	0.1%
1998	67.5%	67.7%	(0.2%)
1999	72.4%	72.7%	(0.3%)
2000	73.0%	73.2%	(0.2%)
2001	67.7%	67.2%	0.5%
2002	70.7%	70.3%	0.4%
2003	74.2%	74.0%	0.2%
2004	73.9%	72.9%	1.0%
2005	73.8%	73.6%	0.2%
2006	70.5%	71.4%*	(0.9%)

* Collection percentage represents the initial forecasted collection percentage

determined at
time of
origination for
2006
originations.

Collection rates during the year ended December 31, 2006 generally exceeded the Company s expectations at December 31, 2005 and had a positive impact on forecasted Consumer Loan collection rates.

Accurately forecasting future collection rates is critical to the Company s success. The risk of a forecasting error declines as Consumer Loans age. For example, the risk of a material forecasting error for business written in 1999 is very small since 98.4% of the total amount forecasted has already been realized. In contrast, the Company s forecast for recent Consumer Loans is less certain. If the Company produces disappointing operating results, it will likely be because the Company overestimated future Consumer Loan performance. Although the Company believes its estimated collection rates are as accurate as possible, there can be no assurance that the Company s estimates will be accurate or that Consumer Loan performance will be as expected.

A wider spread between the forecasted collection rate and the advance rate reduces the Company s risk of credit losses. Because collections are applied to advances on an individual dealer-partner basis, a wide spread does not eliminate the risk of losses, but it does reduce the risk significantly. While the spread has decreased from 2003 to 2006, the Company believes it is still at a sufficient level to minimize the Company s risk of being able to recover the cash advance.

Table of Contents

The Company modified its loan pricing model during the third quarter of 2006. As a result, the composition of new loan originations changed during the year ended December 31, 2006 compared to the same period in 2005 as follows: (1) the average loan size was larger by 6.3%, (2) the average loan term increased from 34 to 37 months, (3) the projected return on capital has decreased by approximately 125 basis points, and (4) the average spread between the advance rate and the expected collection rate has decreased by approximately 300 basis points. The Company also increased its Consumer Loan unit volume by 13.1% and believed this higher volume was due to the pricing modification.

There were no other material changes in credit policy or pricing during 2006, other than routine changes designed to maintain current profitability levels.

Table of Contents

Results of Operations

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

(Dollars in thousands, except per share data)	Year Ended December 31, 2006	% of Revenue	Year Ended December 31, 2005	% of Revenue	Year Ended December 31, 2004	% of Revenue
Revenue:						
Finance charges	$ 188,605	86.0%	$ 176,369	87.6%	$ 150,651	87.5%
License fees	13,589	6.2	9,775	4.9	5,835	3.4
Other income	17,138	7.8	15,124	7.5	15,585	9.1
Total revenue	219,332	100.0	201,268	100.0	172,071	100.0
Costs and expenses:						
Salaries and wages	41,015	18.7	39,093	19.4	35,300	20.5
General and administrative	36,485	16.6	20,834	10.4	20,724	12.0
Sales and marketing	16,624	7.6	14,275	7.1	11,915	6.9
Provision for credit losses	11,006	5.0	5,705	2.8	6,526	3.8
Interest	23,330	10.6	13,886	6.9	11,660	6.8
Other expense	226	0.1	931	0.5	1,270	0.7
Total costs and expenses	128,686	58.6	94,724	47.1	87,395	50.7
Operating income	90,646	41.4	106,544	52.9	84,676	49.3
Foreign currency (loss) gain	(6)		1,812	0.9	1,650	1.0
Income from continuing operations before provision for income taxes	90,640	41.4	108,356	53.8	86,326	50.3
Provision for income taxes	31,793	14.5	40,159	20.0	30,073	17.5
Income from continuing operations	58,847	26.9	68,197	33.8	56,253	32.8
Discontinued operations						
(Loss) gain from discontinued United Kingdom operations	(297)	(0.1)	6,194	3.1	1,556	0.9
(Benefit) provision for income taxes	(90)		1,790	0.9	484	0.3

(Loss) gain from discontinued operations		(207)	(0.1)		4,404	2.2		1,072	0.6
Net income	$	58,640	26.8%	$	72,601	36.0%	$	57,325	33.4%
Net income per common share:									
Basic	$	1.78		$	1.96		$	1.48	
Diluted	$	1.66		$	1.85		$	1.40	
Income from continuing operations per common share:									
Basic	$	1.78		$	1.84		$	1.46	
Diluted	$	1.67		$	1.74		$	1.37	
(Loss) gain from discontinued operations per common share:									
Basic	$	(0.01)		$	0.12		$	0.03	
Diluted	$	(0.01)		$	0.11		$	0.03	
Weighted average shares outstanding:									
Basic		33,035,693			36,991,136			38,617,787	
Diluted		35,283,478			39,207,680			41,017,205	

Table of Contents

Continuing Operations

Year ended December 31, 2006 Compared to Year Ended December 31, 2005

For the year ended December 31, 2006, net income from continuing operations decreased to $58.8 million, or $1.67 per diluted share, compared to $68.2 million, or $1.74 per diluted share, for the same period in 2005. The decrease in net income from continuing operations primarily reflects the following:

General and administrative expense increased $15.7 million primarily due to an $11.2 million increase in the Company s estimated loss related to a pending class action lawsuit in the state of Missouri and lower than normal accounting fees during 2005 as a result of the resolution of a dispute over fees paid to a former auditor.

Interest expense increased $9.4 million primarily due to a 39.0% increase in the amount of average outstanding debt as a result of borrowings used to fund stock repurchases and new Dealer Loan originations. Interest expense also increased as a result of a 220 basis point increase in interest rates partially offset by the decreased impact of fixed fees on the Company s secured financings and line of credit facility due to higher average outstanding borrowings.

Provision for credit losses increased $5.3 million primarily due to an increase in the provision required to maintain the initial yield established at the inception of the Dealer Loan.

Partially offsetting these decreases to income from continuing operations:

Finance charge revenue increased $12.2 million (6.9%) primarily due to a 9.0% increase in the average size of the Dealer Loan portfolio partially offset by a 3.6% decrease in the average yield on Dealer Loans.

Provision for income taxes decreased $8.4 million primarily due to the decrease in income from continuing operations before provision for income taxes.

Finance Charges. Finance charges increased to $188.6 million in 2006 from $176.4 million in 2005 primarily due to a 9.0% increase in the average size of the Dealer Loan portfolio partially offset by a 3.6% decrease in the average yield on Dealer Loans. The Dealer Loan portfolio increased as a result of an increase in the number of active dealer-partners, partially offset by a decrease in the number of transactions per active dealer-partner.

The following table summarizes the changes in active dealer-partners and corresponding Consumer Loan unit volume for the years ended December 31, 2006 and 2005:

	Years Ended December 31,		
	2006	**2005**	**% change**
Consumer Loan unit volume	94,513	83,567	13.1
Active dealer-partners (1)	2,232	1,766	26.4
Average volume per dealer-partner	42.3	47.3	(10.6)
Consumer Loan unit volume from dealer-partners active both periods	75,883	75,480	0.5
Dealer-partners active both periods	1,322	1,322	
Average volume per dealer-partner active both periods	57.4	57.1	0.5
Consumer Loan unit volume from new dealer-partners	17,868	16,278	9.8
New active dealer-partners (2)	873	745	17.2
Average volume per new active dealer-partner	20.5	21.8	(6.0)
Attrition (3)	-9.7%	-5.6%	

(1) Active dealer-partners are dealer-partners who submit at least one Consumer Loan during the period.

(2) New active dealer-partners are dealer-partners that have enrolled in the Company s program and have submitted their first Consumer Loan to the Company during the period.

(3) Attrition is measured according to the following formula: decrease in Consumer Loan unit volume from dealer-partners who submitted at least one Consumer Loan during the comparable period of the prior year but who submitted no Consumer Loans during the current period divided by prior year comparable period

Consumer Loan
unit volume.

In March 2005, the Company implemented a change in policy that allows prospective dealer-partners to enroll in the Company s program without paying the $9,850 enrollment fee. Prospective dealer-partners choosing this option instead agree to allow the Company to keep 50% of the first accelerated dealer holdback payment. This payment, called Portfolio Profit Express, is paid to qualifying dealer-partners after 100 Consumer Loans have been originated and assigned to the Company. While the Company will lose enrollment fee revenue on those dealer-partners choosing this option and not reaching 100 Consumer Loans or otherwise qualifying for a Portfolio Profit Express payment, the Company estimates that it will realize higher per dealer-partner enrollment fee revenue from those dealer-partners choosing this option and qualifying for a Portfolio Profit Express payment. Based on the historical average of Portfolio Profit Express payments, the Company expects average enrollment fee revenue per dealer-partner for those dealer-partners electing the deferred option and reaching 100 Consumer Loans will be approximately $13,000. Approximately 80% of the dealer-partners that enrolled during 2006 took advantage of the deferred enrollment option.

License Fees. License fees increased to $13.6 million in 2006 from $9.8 million in 2005. License fees represent CAPS fees charged to dealer-partners on a monthly basis. CAPS fees are charged to both active and certain inactive dealer-partners. The increase was primarily due to a 43% increase in the number of dealer-partners being charged for CAPS during 2006 compared to the same period in the prior year.

The Company has historically charged dealer-partners a per month license fee for access to CAPS. In accordance with GAAP, this fee has historically been recorded as revenue in the month the fee is charged. Based on feedback received from field sales personnel and dealer-partners, the Company concluded that the way this fee was structured was a significant factor driving higher than desired dealer-partner attrition. Effective January 1, 2007, the Company implemented a change designed to positively impact dealer-partner attrition. The Company will continue to charge a monthly fee of $599 but, instead of collecting the license fee in the current period, the Company will collect the license fee from future dealer holdback payments and recognize it as finance charges over the life of the Dealer Loans.

Under this new program, the Company has concluded it is no longer appropriate from either an accounting or an economic perspective to view the license fees as a current period source of revenue. As a result, starting in the first quarter of 2007, the Company will record license fees on a GAAP basis as a yield adjustment, effectively recognizing these fees over the term of the dealer loan. This GAAP treatment is consistent with the cash economics.

Because the Company will be deferring revenue that was previously recorded immediately, the Company s GAAP financial statements in the near future will be difficult to compare to prior periods for two reasons:

1. As stated above, beginning in the first quarter of 2007, license fees charged will be recognized as revenue over the life of the dealer loan as a yield adjustment, while prior to 2007, license fees were recognized as revenue in the quarter they were charged. This will have the effect in future quarters of reducing license fee revenue from 2006 levels, as only a small portion of license fees will now be recorded as revenue in the quarter they are charged to dealer-partners.

2. Had the Company always accounted for license fees as a yield adjustment, this reduction in revenue (outlined immediately above) would be substantially offset by revenue from license fees charged to dealer-partners in periods prior to 2007. However, since all license fees prior to 2007 have already been recognized as revenue in the period they were charged, it will be several years before this offset occurs in the Company s GAAP financial statements.

To allow shareholders to more precisely track the Company s financial performance and make comparisons between periods possible, the Company will provide adjusted license fees reflecting the amount of revenue if the license fees had always been recorded as a yield adjustment. For the years ended December 31, 2006 and 2005, license fees would have changed as follows:

	As of December 31,	
(Dollars in thousands)	**2006**	**2005**
License fees	$ 13,589	$ 9,775
Yield accounting adjustment	(4,379)	(3,352)
Adjusted license fees	$ 9,210	$ 6,423

Salaries and Wages. Salaries and wages, as a percentage of revenue, decreased to 18.7% in 2006 from 19.4% in 2005. The decrease was primarily related to: (i) a decrease in stock-based compensation expense which was a result of a decline in the number of unvested stock options outstanding and the Company s adoption of SFAS No. 123R which resulted in revised turnover assumptions for the stock options granted during 2002-2004 and (ii) a decrease in support salaries as a percentage of revenue which is consistent with the Company s business plan of growing corporate infrastructure at a rate slower than the growth rate of the Dealer Loan portfolio. The decrease in salaries and wages, as a percentage of revenue, was partially offset by an increase in payroll taxes primarily due to employee and director stock option exercises.

General and Administrative. General and administrative expenses, as a percentage of revenue, increased to 16.6% in 2006 from 10.4% in 2005. The increase, as a percentage of revenue, was primarily due to: (i) an $11.2 million increase in the Company s estimated loss related to a pending class action lawsuit in the state of Missouri, (ii) lower than normal accounting fees during 2005 as a result of the resolution of a dispute over fees paid to a former auditor, (iii) an increase in credit report expenses primarily due to an increase in vendor costs per unit and increased volume, and (iv) an increase in legal expenses related to increased litigation during 2006.

Sales and Marketing. Sales and marketing expenses, as a percentage of revenue, increased to 7.6% in 2006 from 7.1% in 2005. The increase, as a percentage of revenue, was primarily due to an increase in sales commissions, as a percentage of revenue, primarily due to loan origination growth exceeding revenue growth and the impact of a commission plan change during the fourth quarter of 2006, which resulted in an increase in the average commission paid per loan origination.

Provision for Credit Losses. The provision for credit losses increased to $11.0 million in 2006 compared to $5.7 million in 2005. The provision for credit losses consists primarily of a provision to reduce the carrying value of Dealer Loans to maintain the initial yield established at the inception of the Dealer Loan. Additionally, the provision for credit losses includes a provision for losses on Purchased Loans and a provision for losses on notes receivable. The increase in the provision for credit losses in 2006 was primarily due to an increase in the provision required to maintain the initial yield established at the inception of the Dealer Loan.

Interest. Interest expense increased to $23.3 million in 2006 from $13.9 million in 2005 primarily due to a 39.0% increase in the amount of average outstanding debt as a result of borrowings used to fund stock repurchases and new Dealer Loan originations. Interest expense also increased as a result of a 220 basis point increase in interest rates partially offset by the decreased impact of fixed fees on the Company s secured financings and line of credit facility due to higher average outstanding borrowings.

Foreign Exchange. The foreign exchange gain of $1.8 million during 2005 was primarily the result of changes in the fair value of forward contracts entered into during the third quarter of 2003. The Company entered into the forward contracts to ensure that currency fluctuations would not reduce the amount of United States dollars received from the liquidation of the United Kingdom operation. There were no forward contracts outstanding during 2006. In addition, the Company recognized an after-tax foreign currency exchange gain of $0.8 million during the fourth quarter of 2005 following the determination that the liquidation of business in Canada was substantially complete.

Provision for Income Taxes. Provision for income taxes decreased to $31.8 million in 2006 from $40.2 million in 2005 primarily due to a decrease in income from continuing operations before provision for income taxes. The Company s effective tax rate decreased from 37.1% during 2005 to 35.1% during 2006 primarily due to an additional state tax liability recorded in the third quarter of 2005 that was reversed in the second quarter of 2006 as a result of a favorable settlement.

Year ended December 31, 2005 Compared to Year Ended December 31, 2004

For the year ended December 31, 2005, net income from continuing operations increased to $68.2 million, or $1.74 per diluted share, compared to $56.3 million, or $1.37 per diluted share, for the same period in 2004. The increase in net income primarily reflects the following:

Finance charge revenue increased $25.7 million (17.1%) primarily due to an increase in the average size of the Dealer Loan portfolio.

License fees increased $3.9 million primarily due to an increase in the number of dealer-partners being billed for CAPS.

General and administrative expenses, as a percentage of revenue, decreased 1.6% primarily due to a decrease in accounting fees related to the resolution of a dispute over fees paid to a former auditor.

Finance Charges. Finance charges increased to $176.4 million in 2005 from $150.7 million in 2004 primarily due to an increase in the size of the Dealer Loan portfolio resulting from an increase in the number of active dealer-partners, partially offset by a decrease in the number of transactions per active dealer-partner.

The following table summarizes the changes in active dealer-partners and corresponding Consumer Loan unit volume for the years ended December 31, 2005 and 2004:

	Years Ended December 31,		
	2005	**2004**	**% change**
Consumer Loan unit volume	83,567	75,955	10.0
Active dealer-partners (1)	1,766	1,215	45.3
Average volume per dealer-partner	47.3	62.5	(24.3)
Consumer Loan unit volume from dealer-partners active both periods	66,517	71,664	(7.2)
Dealer-partners active both periods	976	976	
Average volume per dealer-partner active both periods	68.2	73.4	(7.2)
Consumer Loan unit volume from new dealer-partners	16,278	14,482	12.4
New active dealer-partners (2)	745	460	62.0
Average volume per new active dealer-partner	21.8	31.5	(30.8)
Attrition (3)	-5.6%	-7.9%	

(1) Active dealer-partners are dealer-partners who submit at least one Consumer Loan during the period.

(2) New active dealer-partners are dealer-partners that have enrolled in the Company s program and have submitted their first Consumer Loan to the Company during the period.

(3) Attrition is measured according to the following formula: decrease in Consumer Loan unit volume from dealer-partners who submitted at least one Consumer Loan during the comparable period of the prior year but who submitted no Consumer Loans during the current period divided by prior year comparable period Consumer Loan unit volume.

The number of new dealer-partner enrollments in 2005 was favorably impacted by a policy implemented in the first quarter of 2005. The policy allows prospective dealer-partners to enroll in the Company s program without paying the $9,850 enrollment fee. Prospective dealer-partners choosing this option instead agree to allow the Company to keep 50% of the first accelerated dealer holdback payment. This payment, called Portfolio Profit Express, is paid to qualifying dealer-partners after 100 Consumer Loans have been originated and assigned to the Company. While the Company will lose enrollment fee revenue on those dealer-partners choosing this option and not reaching 100 Consumer Loans or otherwise qualifying for a Portfolio Profit Express payment, the Company estimates that it will realize higher per dealer-partner enrollment fee revenue from those dealer-partners choosing this option and qualifying for a Portfolio Profit Express payment. Based on the historical average of Portfolio Profit Express payments, the

Company expects average enrollment fee revenue per dealer-partner for those dealer-partners electing the new option and reaching 100 Consumer Loans will be approximately $13,000. Approximately 57% of the dealer-partners that enrolled during 2005 took advantage of this new enrollment option.

License Fees. License fees increased to $9.8 million in 2005 from $5.8 million in 2004 due to an increase in the number of dealer-partners. License fees represent CAPS fees charged to dealer-partners on a monthly basis. The average number of dealer-partners billed for CAPS fees in 2005 was 1,360 compared to 938 in 2004. Effective February 1, 2005, the monthly rate for CAPS fees increased from $499 to $599.

Salaries and Wages. Salaries and wages, as a percentage of revenue, decreased to 19.4% in 2005 from 20.5% in 2004 primarily due to a decrease in servicing salaries, as a percentage of revenue, of 0.5% due to increased operational efficiencies and a decrease in stock-based compensation expense primarily due to a decline in the number of unvested stock options outstanding.

General and Administrative. General and administrative expenses, as a percentage of revenue, decreased to 10.4% in 2005 from 12.0% in 2004. The decrease was primarily due to a decrease in accounting fees related to the resolution of a dispute over fees paid to a former auditor.

Sales and Marketing. Sales and marketing expenses, as a percentage of revenue, were comparable at 7.1% in 2005 and 6.9% in 2004 primarily due to an increase in dealer-partner support products and services, as a percentage of revenue, of 0.4% offset by a decrease in sales commissions, as a percentage of revenue, of 0.3%. The increase in expenses related to dealer-partner support products and services was primarily due to an increase in dealer-partner enrollments. The decrease in sales commissions, as a percentage of revenue, is primarily due to Dealer Loan origination volume growing at a slower rate than finance charge revenue.

Provision for Credit Losses. The provision for credit losses decreased to $5.7 million in 2005 from $6.5 million in 2004. The provision for credit losses consists primarily of a provision to reduce the carrying value of Dealer Loans to maintain the initial yield established at the inception of the Dealer Loan. Additionally, the provision for credit losses includes a provision for losses on Purchased Loans and a provision for losses on notes receivable. The decrease in the provision was primarily due to a decrease in the provision for credit losses required to maintain the initial yield established at the inception of the Dealer Loan and a decline in the Company s automobile leasing business, Canadian automobile financing business and secured lined of credit and floorplan financing products. The Company stopped originating automobile leases and Dealer Loans in Canada. The Company has also significantly reduced its floorplan and secured line of credit portfolios since 2001. The decrease was partially offset by a one-time pre-tax charge of $2.9 million in the third quarter of 2005 related to a reduction in forecasted collection rates resulting from Hurricanes Katrina and Rita.

Interest. Interest expense increased to $13.9 million in 2005 from $11.7 million in 2004. The increase in consolidated interest expense from continuing operations was due to an increase in average outstanding debt as a result of stock repurchases in the third quarter of 2004 and an increase in the weighted average interest rate to 7.4% in 2005 from 7.0% in 2004. The increase in the interest rate is primarily the result of increased market rates partially offset by the decreased impact of fixed fees on the Company s secured financing and line of credit facility due to higher average outstanding borrowings.

Provision for Income Taxes. The effective tax rates increased to 37.1% in 2005 from 34.8% in 2004 primarily due to a change made to the Company s tax structure in 2004 to treat the Company s foreign subsidiaries as branches subject to United States jurisdiction. The effective tax rate also increased due to an additional state tax liability recorded in the third quarter of 2005.

Critical Accounting Estimates

The Company s consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. On an ongoing basis, the Company evaluates its estimates, including those related to the allowance for credit losses, finance charge revenue, stock-based compensation expense, contingencies, and taxes. The Company believes the following critical accounting policies involve a high degree of judgment and complexity, and the use of different estimates or assumptions could produce materially different financial results.

Finance Charge Revenue

Balance Sheet Caption:	Loans receivable
Income Statement Caption:	Finance charges
Nature of Estimates Required:	Estimating revenue recognition using the interest rate method of accounting.
Assumptions and Approaches Used:	The Company recognizes finance charge income under an approach similar to the provisions of SOP 03-3 Accounting for Certain Loans or Debt Securities Acquired in a Transfer. SOP 03-3 requires the Company to recognize finance charges under the interest method such that revenue is recognized on a level yield basis based upon forecasted cash flows. As the forecasted cash flows change over time, the Company prospectively adjusts the rate upwards for positive changes but recognizes impairment for negative changes in the current period.
Key Factors:	Variances in the amount and timing of future collections and dealer holdback payments from current estimates could materially impact earnings in future periods.

Allowance for Credit Losses

Balance Sheet Caption:	Allowance for credit losses
Income Statement Caption:	Provision for credit losses
Nature of Estimates Required:	Estimating the amount and timing of future collections and dealer holdback payments.
Assumptions and Approaches Used:	The Company maintains an allowance for credit losses for any Dealer Loan balance that, based on current expectations, is not expected to achieve the weighted average initial yield established at the inception of the Dealer Loan. The Company compares the present value (discounted at the weighted average initial yield) of estimated future collections less the present value of the estimated related dealer holdback payments for each Dealer Loan to the recorded net investment in that Dealer Loan. If the present value of such cash flows is less than the carrying amount of the Dealer Loan, an allowance for credit losses is established to reduce the carrying amount to the calculated present value. The estimates of future collections and the related dealer holdback payments use various assumptions based on a dealer-partner s actual loss data and the Company s historical loss and collection experience. At December 31, 2006, a 1% decline in the forecasted future collections would result in approximately a $3.9 million pre-tax charge to the provision for credit losses. For additional information, see Note 1 to the consolidated financial statements, which is incorporated herein by reference.
Key Factors:	

	Variances in the amount and timing of future collections and dealer holdback payments from current estimates could materially impact earnings in future periods.
Stock-Based Compensation Expense	
Balance Sheet Caption:	Paid-in capital
Income Statement Caption:	Salaries and Wages
Nature of Estimates Required:	Compensation expense for stock options is based on the fair value of the options on the date of grant, which is estimated by the Company, and is recognized over the expected vesting period of the options. The Company also estimates expected vesting dates and expected forfeiture rate of performance-based restricted stock grants.

Assumptions and Approaches Used:	The Company uses the Black-Scholes option pricing model to estimate the fair value of stock option grants. This model calculates the fair value using various assumptions, including the expected life of the option, the expected volatility of the underlying stock, and the expected dividend yield on the underlying stock. In recognizing stock-based compensation expense, the Company makes assumptions regarding the expected forfeiture rate of stock options and restricted stock and the expected vesting date of performance-based options and restricted stock grants. For additional information, see Notes 1 and 9 to the consolidated financial statements, which are incorporated herein by reference.
Key Factors:	Changes in the expected vesting dates of performance-based stock options and restricted stock would impact the amount and timing of stock-based compensation expense recognized in future periods.

Litigation and Contingent Liabilities

Balance Sheet Caption:	Accounts payable and accrued liabilities
Income Statement Caption:	General and administrative expense
Nature of Estimates Required:	Estimating the likelihood of adverse legal judgments and any resulting damages owed.
Assumptions and Approaches Used:	The Company, with assistance from its legal counsel, determines if the likelihood of an adverse judgment for various claims and litigation is remote, reasonably possible, or probable. To the extent the Company believes an adverse judgment is probable and the amount of the judgment is estimable, the Company recognizes a liability. For information regarding the potential various consumer claims against the Company, see Note 12 to the consolidated financial statements, which is incorporated herein by reference.
Key Factors:	Negative variances in the ultimate disposition of claims and litigation outstanding from current estimates could result in additional expense in future periods.

Taxes

Balance Sheet Captions:	Deferred income taxes, net Income taxes receivable Accounts payable and accrued liabilities
Income Statement Caption:	Provision for income taxes
Nature of Estimates Required:	Estimating the recoverability of deferred tax assets.
Assumptions and Approaches Used:	The Company, based on historical and projected future financial results by tax jurisdiction, determines if it is more likely than not a deferred tax asset will be realized. To the extent the Company believes the recovery of all or a portion of a deferred tax asset is not likely, a valuation allowance is established. For additional information, see Note 8 to the consolidated financial statements, which is incorporated herein by reference.
Key Factors:	Changes in tax laws and variances in projected future results from current estimates that impact judgments made on valuation allowances could impact the Company s provision for income taxes in future periods.

Liquidity and Capital Resources

The Company s primary sources of capital are cash flows from operating activities, collections of Consumer Loans receivable and borrowings under the Company s lines of credit and secured financings. The Company s principal need for capital is to fund Dealer Loan originations, for the payment of dealer holdback, and to fund stock repurchases. In addition, on February 9, 2007 the Company signed a Memorandum of Understanding to settle a consumer class action lawsuit. Credit Acceptance has agreed to pay $12.5 million in full and final settlement of all claims against the Company. The settlement is subject to court approval. The Company estimates that the final court approval will not occur for three to six months from the date of this report. For additional information see Note 12 to the consolidated financial statements, which is incorporated herein by reference.

The Company s cash flow requirements are dependent on levels of Dealer Loan originations. In 2006, the Company experienced an increase in Dealer Loan originations from 2005 primarily due to an increase in the number of active dealer-partners due to increased dealer-partner enrollments. The Company s restricted cash and cash equivalents increased primarily due to having $336.1 million in additional assets pledged to securitizations. Under the Company s securitization agreements the Company is required to remit all collections related to these assets to restricted accounts.

The Company currently finances its operations through: (i) a revolving line of credit; (ii) secured financings; (iii) a mortgage loan; and (iv) capital lease obligations. For information regarding these financings and the covenants included in the related documents, see Note 6 to the consolidated financial statements, which is incorporated herein by reference. As of December 31, 2006, the Company is in compliance with various restrictive debt covenants that require the maintenance of certain financial ratios and other financial conditions. The most restrictive covenants require a minimum ratio of the Company s assets to debt and its earnings before interest, taxes and non-cash expenses to fixed charges. The covenants also limit the maximum ratio of the Company s debt to tangible net worth and the Company must also maintain a specified minimum level of net worth, which may indirectly limit the payment of dividends on common stock.

The Company s total balance sheet indebtedness increased to $392.2 million at December 31, 2006 from $146.9 million at December 31, 2005. In addition to the balance sheet indebtedness as of December 31, 2006, the Company also has contractual obligations resulting in future minimum payments under operating leases.

A summary of the total future contractual obligations requiring repayments as of December 31, 2006 is as follows (in thousands):

	Payments due by period				
	Total	**< 1 year**	**1-3 years**	**3-5 years**	**> 5 years**
Contractual Obligations					
Long-term debt obligations (1)	$ 390,368	$ 92,209	$ 298,159	$	$
Capital lease obligations	1,807	639	1,168		
Operating lease obligations	1,538	666	872		
Purchase obligations					
Other long-term obligations					
Total contractual obligations	$ 393,713	$ 93,514	$ 300,199	$	$

(1) Long-term debt obligations included in the above table consists solely of principal repayments. The

Company is also obligated to make interest payments at the applicable interest rates, as discussed in Note 6 in the consolidated financial statements, which is incorporated herein by reference. Based on the amount of debt outstanding and the interest rates as of December 31, 2006, interest is expected to be approximately $15.7 million during 2007 and $4.9 million during 2008 and 2009.

Repurchase and Retirement of Common Stock. For information regarding the Company s stock repurchase program, see Note 9 to the consolidated financial statements, which is incorporated herein by reference.

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

Market Risk

The Company is exposed primarily to market risks associated with movements in interest rates. The Company s policies and procedures prohibit the use of financial instruments for trading purposes. A discussion of the Company s accounting policies for derivative instruments is included in the Summary of Significant Accounting Policies in Note 1 to the consolidated financial statements, which is incorporated herein by reference.

Interest Rate Risk. The Company relies on various sources of financing, some of which are at floating rates of interest and expose the Company to risks associated with increases in interest rates. The Company manages such risk primarily by entering into interest rate cap agreements.

As of December 31, 2006, the Company had $38.4 million of floating rate debt outstanding on its bank credit facility, with no interest rate cap protection. As of December 31, 2006, the Company had $171.0 million in floating rate debt outstanding under its secured warehouse financing, with an interest rate cap of 6.75%. In addition, as of December 31, 2006 the Company had $174.1 million in fixed rate debt outstanding under its 144 term asset backed secured financings. Based on the difference between the Company s rates on its warehouse financing at December 31, 2006 and the interest rate cap, the Company s maximum interest rate risk on the secured warehouse financing is 1.4%. This maximum interest rate risk would reduce annual after-tax earnings by approximately $1.5 million in 2006. For every 1% increase in rates on the Company s bank credit facility, annual after-tax earnings would decrease by approximately $0.2 million in 2006. This analysis assumes the Company maintains a level amount of floating rate debt.

Table of Contents

New Accounting Pronouncements

Stock-based Compensation. On January 1, 2006, the Company adopted revised Statement of Financial Accounting Standards (SFAS) No. 123 (SFAS No. 123R), Share-Based Payment under the modified prospective application method. The Company had previously adopted the fair value recognition provisions of SFAS No. 123, Accounting for Stock-Based Compensation , under the retroactive restatement transition method in 2003. Adoption of SFAS No. 123R primarily resulted in a change in the Company s estimated forfeitures for unvested stock-based compensation awards, which resulted in a cumulative reversal of stock-based compensation expense of $0.4 million for the quarter ended March 31, 2006.

Accounting for Uncertainty in Income Taxes. On July 13, 2006, the FASB issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes An Interpretation of FASB Statement No. 109 (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an entity s financial statements in accordance with FASB Statement No. 109, Accounting for Income Taxes and prescribes a recognition threshold and measurement attributes for financial statement disclosure of tax positions taken or expected to be taken on a tax return. Under FIN 48, the impact of an uncertain income tax position on the income tax return must be recognized at the largest amount that is more-likely-than-not to be sustained upon audit by the relevant taxing authority. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained. Additionally, FIN 48 provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company adopted the provisions of FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes, on January 1, 2007. The cumulative effect of implementation of FIN 48, is approximately a $0.1 million increase in the liability for unrecognized tax benefits, which will be accounted for as a decrease in the January 1, 2007, balance of retained earnings.

Financial Statement Misstatements. In September 2006, the SEC staff issued Staff Accounting Bulletin No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements (SAB 108). SAB 108 was issued to provide consistency between how registrants quantify financial statement misstatements. The Company initially applied SAB 108 in connection with the preparation of the Company s annual financial statements for the year ending December 31, 2006, and it did not have any impact on the Company s financial statements.

Forward-Looking Statements

The Company makes forward-looking statements in this report and may make such statements in future filings with the Securities and Exchange Commission (SEC). It may also make forward-looking statements in its press releases or other public or shareholder communications. The Company s forward-looking statements are subject to risks and uncertainties and include information about its expectations and possible or assumed future results of operations. When the Company uses any of the words may, will, should, believes, expects, anticipates, assumes, fore estimates, intends, plans or similar expressions, it is making forward-looking statements.

The Company claims the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995 for all of its forward-looking statements. These forward-looking statements represent the Company s outlook only as of the date of this report. While the Company believes that its forward-looking statements are reasonable, actual results could differ materially since the statements are based on our current expectations, which are subject to risks and uncertainties. Factors that might cause such a difference include, but are not limited to, the factors set forth under Item 1A. Risk Factors elsewhere in this report and the risks and uncertainties discussed in the Company s other reports filed or furnished from time to time with the SEC.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The information called for by Item 7A is incorporated by reference from the information in Item 7 under the caption Market Risk in this Form 10-K.

Table of Contents

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

	Page
Report of Independent Registered Public Accounting Firm	35
Consolidated Balance Sheets as of December 31, 2006 and 2005	36
Consolidated Statements of Income for the years ended December 31, 2006, 2005, and 2004	37
Consolidated Statements of Shareholders Equity for the years ended December 31, 2006, 2005, and 2004	38
Consolidated Statements of Cash Flows for the years ended December 31, 2006, 2005, and 2004	39
Notes to the Consolidated Financial Statements	40

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and
Shareholders of Credit Acceptance Corporation

We have audited the accompanying consolidated balance sheets of Credit Acceptance Corporation and Subsidiaries (the Company) as of December 31, 2006 and 2005, and the related consolidated statements of income, shareholders equity and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these 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 Credit Acceptance Corporation and Subsidiaries as of December 31, 2006 and 2005, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2006 in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Credit Acceptance Corporation s internal control over financial reporting as of December 31, 2006, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated March 2, 2007 expressed an unqualified opinion on management s assessment of the effectiveness of the Company s internal control over financial reporting and an unqualified opinion on the effectiveness of the Company s internal control over financial reporting.

/s/ GRANT THORNTON LLP
Southfield, Michigan
March 2, 2007

Table of Contents

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except per share data)	December 31, 2006	2005
ASSETS:		
Cash and cash equivalents	$ 8,528	$ 7,090
Restricted cash and cash equivalents	45,609	13,473
Restricted securities available for sale	3,564	3,345
Loans receivable (including $23,038 and $24,765 from affiliates as of December 31, 2006 and 2005, respectively)	754,571	694,939
Allowance for credit losses	(128,791)	(131,411)
Loans receivable, net	625,780	563,528
Property and equipment, net	16,203	17,992
Income taxes receivable	11,734	4,022
Other assets	13,795	9,944
Total Assets	$ 725,213	$ 619,394
LIABILITIES AND SHAREHOLDERS EQUITY:		
Liabilities:		
Accounts payable and accrued liabilities	$ 78,294	$ 55,705
Line of credit	38,400	36,300
Secured financing	345,144	101,500
Mortgage note and capital lease obligations	8,631	9,105
Deferred income taxes, net	44,397	43,758
Total Liabilities	514,866	246,368
Contingencies (Note 12)		
Shareholders Equity:		
Preferred stock, $.01 par value, 1,000,000 shares authorized, none issued		
Common stock, $.01 par value, 80,000,000 shares authorized, 30,179,959 and 37,027,286 shares issued and outstanding at December 31, 2006 and 2005, respectively	302	370
Paid-in capital	828	29,746
Unearned stock-based compensation		(1,566)
Retained earnings	209,253	344,513
Accumulated other comprehensive loss, net of tax of $19 and $22 at December 31, 2006 and 2005, respectively	(36)	(37)
Total Shareholders Equity	210,347	373,026

Total Liabilities and Shareholders Equity	$ 725,213	$ 619,394

See accompanying notes to consolidated financial statements.

Table of Contents

CONSOLIDATED STATEMENTS OF INCOME

	(Dollars in Thousands, Except for Per Share Data) For the Years Ended December 31,		
	2006	2005	2004
Revenue:			
Finance charges	$ 188,605	$ 176,369	$ 150,651
License fees	13,589	9,775	5,835
Other income	17,138	15,124	15,585
Total revenue	219,332	201,268	172,071
Costs and expenses:			
Salaries and wages	41,015	39,093	35,300
General and administrative	36,485	20,834	20,724
Sales and marketing	16,624	14,275	11,915
Provision for credit losses	11,006	5,705	6,526
Interest	23,330	13,886	11,660
Other expense	226	931	1,270
Total costs and expenses	128,686	94,724	87,395
Operating income	90,646	106,544	84,676
Foreign currency (loss) gain	(6)	1,812	1,650
Income from continuing operations before provision for income taxes	90,640	108,356	86,326
Provision for income taxes	31,793	40,159	30,073
Income from continuing operations	58,847	68,197	56,253
Discontinued operations			
(Loss) gain from discontinued United Kingdom operations	(297)	6,194	1,556
(Benefit) provision for income taxes	(90)	1,790	484
(Loss) gain on discontinued operations	(207)	4,404	1,072
Net income	$ 58,640	$ 72,601	$ 57,325

Net income per common share:						
Basic	$	1.78	$	1.96	$	1.48
Diluted	$	1.66	$	1.85	$	1.40
Income from continuing operations per common share:						
Basic	$	1.78	$	1.84	$	1.46
Diluted	$	1.67	$	1.74	$	1.37
(Loss) gain from discontinued operations per common share:						
Basic	$	(0.01)	$	0.12	$	0.03
Diluted	$	(0.01)	$	0.11	$	0.03
Weighted average shares outstanding:						
Basic		33,035,693		36,991,136		38,617,787
Diluted		35,283,478		39,207,680		41,017,205

See accompanying notes to consolidated financial statements.

Table of Contents

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY
(In Thousands)

	Total Shareholders Equity	Comprehensive Income (Loss)	Common Stock Number	Common Stock Amount	Paid-In Capital	Unearned Stock Compensation	Retained Earnings	Accumulated Other Comprehensive Income (Loss)
Balance, January 1, 2004	$ 343,295		42,128	$ 421	$ 125,077	$	$ 214,587	$ 3,210
Comprehensive income:								
Net income	57,325	$ 57,325					57,325	
Other comprehensive loss:								
Unrealized loss on securities available for sale, net of tax of $2	(4)	(4)						(4)
Foreign currency translation adjustment, net of tax of ($1,760)	(237)	(237)						(237)
Total comprehensive income		$ 57,084						
Stock-based compensation	2,725				2,725			
Repurchase and retirement of common stock	(107,236)		(5,752)	(57)	(107,179)			
Stock options exercised	5,022		521	5	5,017			
Balance, December 31, 2004	300,890		36,897	369	25,640		271,912	2,969
Comprehensive income:								
Net income	72,601	$ 72,601					72,601	
Other comprehensive								

loss:								
Unrealized loss on securities available for sale, net of tax of $20	(33)	(33)						(33)
Foreign currency translation adjustment, net of tax of $0	(2,973)	(2,973)						(2,973)
Total comprehensive income		$ 69,595						
Stock-based compensation	2,331				1,936	395		
Issuance of restricted stock, net of forfeitures			99	1	1,960	(1,961)		
Stock options exercised	210		31		210			
Balance, December 31, 2005	373,026		37,027	370	29,746	(1,566)	344,513	(37)
Adjustment due to SFAS 123R adoption - modified prospective application					(1,566)	1,566		
Comprehensive income:								
Net income	58,640	$ 58,640					58,640	
Other comprehensive income:								
Unrealized gain on securities available for sale, net of tax of $3	1	1						1
Total comprehensive income		$ 58,641						
Stock-based compensation	87				87			

Issuance of restricted stock, net of forfeitures		47					
Repurchase of common stock	(247,168)	(8,796)	(87)	(53,181)		(193,900)	
Stock options exercised	12,091	1,902	19	12,072			
Tax benefit for exercised stock options	13,670			13,670			
Balance, December 31, 2006	$ 210,347	30,180	$ 302	$ 828	$	$ 209,253	$ (36)

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	(Dollars In Thousands) For the Years Ended December 31,		
	2006	2005	2004
Cash Flows From Operating Activities:			
Net Income	$ 58,640	$ 72,601	$ 57,325
Adjustments to reconcile cash provided by operating activities:			
Provision for credit losses	11,006	3,979	5,757
Depreciation	4,624	5,209	5,781
(Gain) loss on retirement of property and equipment	(271)	76	230
Foreign currency gain on forward contracts		(1,033)	(1,661)
Provision for deferred income taxes	636	11,961	12,859
Stock-based compensation	87	2,331	2,725
Gain on sale of United Kingdom loan portfolio		(3,033)	
Change in operating assets and liabilities:			
Accounts payable and accrued liabilities	22,589	7,354	11,715
Income taxes receivable/payable	(7,712)	5,422	(11,530)
Other assets	(3,425)	(490)	(427)
Net cash provided by operating activities	86,174	104,377	82,774
Cash Flows From Investing Activities:			
(Increase) decrease in restricted cash	(32,136)	10,454	13,348
Purchases of restricted securities available for sale	(795)	(3,239)	(934)
Proceeds from sale of restricted securities available for sale	302	742	
Maturities of restricted securities available for sale	278	27	
Principal collected on loans receivable	551,792	468,273	397,091
Advances to dealers and accelerated payments of dealer holdback	(532,869)	(461,877)	(427,866)
Originations of purchased loans	(25,562)	(13,354)	(7,938)
Payments of dealer holdback	(70,110)	(52,887)	(34,421)
Proceeds from the sale of United Kingdom loan portfolio		4,297	
Purchases of property and equipment	(1,536)	(2,863)	(3,567)
Net change in floorplan receivables, notes receivable and lines of credit	3,050	600	1,048
Net cash used in investing activities	(107,586)	(49,827)	(63,239)
Cash Flows From Financing Activities:			
Borrowings under line of credit	414,630	250,700	314,000
Repayments under line of credit	(412,530)	(222,100)	(306,300)
Proceeds from secured financings	678,500	120,500	288,000
Repayments of secured financings	(434,856)	(195,000)	(212,000)
Principal payments under mortgage and capital lease obligations	(1,502)	(1,296)	(2,821)
Proceeds from mortgage note refinancing			3,540
Repurchase of common stock	(247,168)		(107,236)

Proceeds from stock options exercised	12,091	210	5,022
Excess tax benefits from stock-based compensation plans	13,670		
Net cash provided by (used in) financing activities	22,835	(46,986)	(17,795)
Effect of exchange rate changes on cash	15	(1,088)	(2,262)
Net increase (decrease) in cash and cash equivalents	1,438	6,476	(522)
Cash and cash equivalents, beginning of period	7,090	614	1,136
Cash and cash equivalents, end of period	$ 8,528	$ 7,090	$ 614
Supplemental Disclosure of Cash Flow Information:			
Cash paid during the period for interest	$ 23,056	$ 13,244	$ 10,920
Cash paid during the period for income taxes	$ 25,427	$ 23,454	$ 26,855
Supplemental Disclosure of Non-Cash Transactions:			
Property and equipment acquired through capital lease obligations	$ 1,785	$ 531	$ 2,038
Issuance of restricted stock, net of forfeitures	$ 1,303	$ 1,961	$

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of Business

Principal Business. Since 1972, Credit Acceptance (the Company or Credit Acceptance) has provided auto loans to consumers, regardless of their credit history. The Company s product is offered through a nationwide network of automobile dealers who benefit from sales of vehicles to consumers who otherwise could not obtain financing; from repeat and referral sales generated by these same customers; and from sales to customers responding to advertisements for the Company s product, but who actually end up qualifying for traditional financing.

The Company refers to dealers who participate in its program and who share its commitment to changing consumers lives as dealer-partners . Upon enrollment in the Company s financing program, the dealer-partner enters into a dealer servicing agreement with Credit Acceptance that defines the legal relationship between Credit Acceptance and the dealer-partner. The dealer servicing agreement assigns the responsibilities for administering, servicing, and collecting the amounts due on retail installment contracts (referred to as Consumer Loans) from the dealer-partners to the Company.

If the Company discovers a misrepresentation by the dealer-partner relating to a Consumer Loan assigned to the Company, the Company can demand that the Consumer Loan be repurchased for the current balance of the Consumer Loan less the amount of any unearned finance charge plus the applicable termination fee, which is generally $500. Upon receipt of such amount in full, the Company will reassign the Consumer Loan and its security interest in the financed vehicle to the dealer-partner. The dealer-partner can also opt to repurchase Consumer Loans at their own discretion.

The Company is an indirect lender from a legal perspective, meaning the Consumer Loan is originated by the dealer-partner and immediately assigned to the Company. Typically, the compensation paid to the dealer-partner in exchange for the Consumer Loan is paid in two parts. A portion of the compensation is paid at the time of origination, and a portion is paid over time. The amount paid at the time of origination is called an advance; the portion paid over time is based on the performance of the loan and is called dealer holdback (dealer holdback).

For accounting purposes, the transactions described above are not considered to be loans to consumers. Instead, the Company s accounting reflects that of a lender to the dealer-partner. This classification for accounting purposes is primarily a result of (i) the dealer-partner s financial interest in the Consumer Loan and (ii) certain elements of the Company s legal relationship with the dealer-partner. The cash amount advanced to the dealer-partner is recorded as an asset on the Company s balance sheet. The aggregate amount of all advances to an individual dealer-partner, plus accrued income, less repayments comprises the amount recorded in Loans receivable.

A small percentage of Consumer Loans in the United States are assigned to the Company in exchange for a single payment. Because the dealer-partner does not retain a financial interest in loans acquired in this manner, these loans are considered to be Purchased Loans (Purchased Loans) for accounting purposes.

Loans receivable. At the time of acceptance, Consumer Loans that meet certain criteria are eligible for a non-recourse cash payment to the dealer-partner (referred to as an advance), which is computed on a formula basis. Upon acceptance of an assigned Consumer Loan, the Company records the cash amount advanced to the dealer-partner as a Dealer Loan (Dealer Loan) classified in Loans receivable in the consolidated financial statements.

Cash advanced to dealer-partners is automatically assigned to the originating dealer-partner s open pool of business. At the dealer-partner s option, a pool containing at least 100 Consumer Loans can be closed and subsequent advances assigned to a new pool. All advances due from a dealer-partner are secured by the future collections on the dealer-partner s portfolio of Consumer Loans that have been assigned to the Company. Net collections on all related Consumer Loans within the pool, after payment of the Company s servicing fee and reimbursement of certain collection costs, are applied to reduce the aggregate advance balance owing against those Consumer Loans. Once the advance balance has been repaid, the dealer-partner is entitled to receive future collections from Consumer Loans within that pool, after payment of the Company s servicing fee and reimbursement of certain collection costs. If the collections on Consumer Loans from a dealer-partner s pool are not sufficient to repay the advance balance, the dealer-partner will not receive the portion of compensation that is paid based on the performance of the Consumer Loans (dealer holdback). Additionally, for dealer-partners with more than one pool, the pools are cross-collateralized

so the performance of other pools is considered in determining eligibility for dealer holdback payments.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Businesses in Liquidation. The Company sold its United Kingdom Consumer Loan portfolio on December 30, 2005. The selling price was approximately $4.3 million resulting in a pre-tax gain of approximately $3.0 million.

Effective June 30, 2003, the Company decided to stop originating Dealer Loans in Canada. Since Dealer Loans originated in Canada are serviced in the United States, the Company evaluated cash flows related to the Canadian operation based on the same collection rate assumptions as were used before the decision to liquidate. Based upon management s analysis as of December 31, 2006, no reduction of the carrying value of the Canadian Dealer Loan portfolio is required.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany transactions have been eliminated. The Company s primary subsidiaries are: Buyer s Vehicle Protection Plan, Inc., CAC of Canada Company, and Vehicle Remarketing Services, Inc.

Reportable Business Segments

The Company is organized into two primary business segments: United States and Other. See Note 10 Business Segment Information for information regarding the Company s reportable segments.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP), requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The accounts which are subject to significant estimation include the allowance for credit losses, finance charge revenue, stock-based compensation expense, impairment of various assets, contingencies, and taxes. Actual results could materially differ from those estimates.

Cash and Cash Equivalents

Cash equivalents consist of readily marketable securities with original maturities at the date of acquisition of three months or less.

Restricted Cash and Cash Equivalents

Restricted cash and cash equivalents consist of amounts held in accordance with secured financing and vehicle service contract trust arrangements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Restricted Securities Available for Sale

Restricted securities consist of the amounts held in accordance with vehicle service contract trust agreements. The Company determines the appropriate classification of its investments in debt and equity securities at the time of purchase and reevaluates such determinations at each balance sheet date. Debt securities for which the Company does not have the intent or ability to hold to maturity are classified as available for sale, and stated at fair value with unrealized gains and losses, net of income taxes included in the determination of comprehensive income and reported as a component of shareholders equity.

Restricted available-for-sale securities consist of the following:

	As of December 31, 2006			
(Dollars in thousands)	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
US Government and agency securities	$ 1,578	$	$ (8)	$ 1,570
Corporate bonds	2,041		(47)	1,994
Total restricted securities available for sale	$ 3,619	$	$ (55)	$ 3,564

	As of December 31, 2005			
(Dollars in thousands)	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
US Government and agency securities	$ 1,336	$	$ (14)	$ 1,322
Corporate bonds	2,068		(45)	2,023
Total restricted securities available for sale	$ 3,404	$	$ (59)	$ 3,345

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

	As of December 31,			
	2006		2005	
(Dollars in thousands)	Cost	Estimated Fair Value	Cost	Estimated Fair Value
Contractual Maturity				
Within one year	$ 898	$ 893	$	$
Over one year to five years	2,721	2,671	3,028	2,971
Over five years to ten years			376	374
Total restricted securities available for sale	$ 3,619	$ 3,564	$ 3,404	$ 3,345

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Finance Charges

The Company recognizes finance charge income in a manner consistent with the provisions of the American Institute of Certified Public Accountant s Statement of Position (SOP) 03-3 Accounting for Certain Loans or Debt Securities Acquired in a Transfer. SOP 03-3 requires the Company to recognize finance charges under the interest method such that revenue is recognized on a level yield basis based upon forecasted cash flows. As the forecasted cash flows change, the Company would prospectively adjust the yield upwards for positive changes but would recognize impairment for negative changes in the current period.

Buyers Vehicle Protection Plan, Inc. (BVPP), a wholly owned subsidiary of the Company, has relationships with third party vehicle service contract administrators (TPAs) whereby the TPAs process claims on vehicle service contracts underwritten by third party insurers. BVPP receives a commission for all such vehicle service contracts sold by its dealer-partners where the vehicle service contract is financed by the Company, and does not bear any risk of loss for claims covered on these third party service contracts. The commission is included in the purchase price of the vehicle service contract included in the Consumer Loan. The Company advances to dealer-partners an amount based on the purchase price of the vehicle service contract on Consumer Loans accepted by the Company that include vehicle service contracts.

The Company has two agreements with TPAs with the following attributes: (i) the agreements provide a commission to the Company on all vehicle service contracts sold by its dealer-partners, regardless of whether the vehicle service contract is financed by the Company, (ii) the Company experiences a higher commission on vehicle service contracts financed by the Company, and (iii) the agreements allow the Company to participate in underwriting profits depending on the level of future claims paid. The Company will be eligible in 2007 to receive profits related to 2004. The two agreements also require that net premiums on the vehicle service contracts be placed in trust accounts by the TPA. Funds in the trust accounts are utilized by the TPA to pay claims on the vehicle service contracts. Underwriting profits, if any, on the vehicle service contracts are distributed to the Company after the term of the vehicle service contracts have expired provided certain loss rates are met. Under FASB Interpretation No. 46, Consolidation of Variable Interest Entities (FIN 46), the Company is considered the primary beneficiary of the trusts. As a result, the assets and liabilities of the trusts have been consolidated on the Company s balance sheet. As of December 31, 2006, the trusts had $18.2 million in assets available to pay claims and a related claims reserve of $17.7 million. The trust assets are included in cash and cash equivalents, restricted cash and cash equivalents, and restricted securities available for sale. The claims reserve is included in accounts payable and accrued liabilities in the consolidated balance sheets. A third party insures claims in excess of funds in the trust accounts.

The Company recognizes the commission received from the TPAs for contracts financed by the Company as part of finance charges on a level yield basis based upon forecasted cash flows. Commissions on contracts not financed by the Company are recognized as finance charge income at the time the commissions are received. Revenue related to underwriting profits is recognized in the period received.

During the first quarter of 2005, the Company began offering Guaranteed Asset Protection (GAP) debt cancellation terms in its contracts. GAP provides the consumer protection by paying the difference between the loan balance and the consumer s insurance coverage limit in the event the vehicle is totaled or stolen. The Company receives a fee for every GAP product sold by its dealer-partners. The Company recognizes the commission received for GAP products as part of finance charges on a level yield basis based upon forecasted cash flows.

Loans Receivable and Allowance for Credit Losses

The Company records the amount advanced to the dealer-partner as a Dealer Loan. The Dealer Loan is increased as revenue is recognized and decreased as collections are received. The Company follows an approach similar to the provisions of SOP 03-3 in determining its allowance for credit losses. Consistent with SOP 03-3, an allowance for credit losses is maintained at an amount that reduces the net asset value (Dealer Loan balance less the allowance) to the value of forecasted future cash flows discounted at the yield established at the inception of the Dealer Loan. This allowance is calculated on a dealer-partner by dealer-partner basis. The discounted value of future cash flows is comprised of estimated future collections on the Consumer Loans, less any estimated dealer holdback payments.

In estimating future collections and dealer holdback payments for each dealer-partner, the Company considers: (i) a dealer-partner s actual loss data on a static pool basis and (ii) the Company s historical loss and collection experience. The Company s

43

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

collection forecast for each dealer-partner is updated monthly and considers the most recent static pool data available for each dealer-partner and the Company s entire portfolio of Consumer Loans.

Cash flows from any individual Dealer Loan are often different than estimated cash flows at Dealer Loan inception. If such difference is favorable, the difference is recognized into income over the re