
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549**

FORM 10-Q

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

For the quarterly period ended September 30, 2004

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

For the transition period from _____ to _____.

Commission file number: 1-11416

CONSUMER PORTFOLIO SERVICES, INC.

(Exact name of registrant as specified in its charter)

California
(State or other jurisdiction of
incorporation or organization)

33-0459135
(IRS Employer
Identification No.)

16355 Laguna Canyon Road, Irvine, California
(Address of principal executive offices)

92618
(Zip Code)

Registrant's telephone number: (949) 753-6800

Former name, former address and former fiscal year, if changed since last report: N/A

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

Indicate by check mark whether the registrant is an accelerated filer (as defined by Rule 12b-2 of the Exchange Act). Yes No

As of November 9, 2004 the registrant had 21,418,689 common shares outstanding.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES
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Item 1. Financial Statements**CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share and per share data)**

	<u>September 30,</u> <u>2004</u>	<u>December 31,</u> <u>2003</u>
ASSETS		
Cash	\$ 10,952	\$ 33,209
Restricted cash	113,816	67,277
Finance receivables	524,950	302,078
Less: Allowance for finance credit losses	(39,028)	(35,889)
Finance receivables, net	<u>485,922</u>	<u>266,189</u>
Servicing fees receivable	3,441	3,942
Residual interest in securitizations	68,714	111,702
Furniture and equipment, net	1,650	826
Deferred financing costs	5,996	1,529
Other assets	15,335	7,796
	<u>\$ 705,826</u>	<u>\$ 492,470</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities		
Accounts payable and accrued expenses	\$ 24,081	\$ 22,920
Warehouse lines of credit	16,521	33,709
Tax liabilities, net	2,949	2,768
Capital lease obligation	391	-
Notes payable	1,593	3,330
Residual interest financing	27,311	-
Securitization trust debt	477,891	245,118
Senior secured debt	59,829	49,965
Subordinated debt	15,000	35,000
Related party debt	-	17,500
	<u>625,566</u>	<u>410,310</u>
Shareholders' Equity		
Preferred stock, \$1 par value; authorized 5,000,000 shares; none issued	-	-
Series A preferred stock, \$1 par value; authorized 5,000,000 shares; 3,415,000 shares issued; none outstanding	-	-
Common stock, no par value; authorized 30,000,000 shares; 21,403,409 and 20,588,924 shares issued and outstanding at September 30, 2004 and December 31, 2003, respectively	65,894	64,397
Retained earnings	17,350	20,992
Comprehensive loss - minimum pension benefit obligation, net	(2,426)	(2,426)
Deferred compensation	(558)	(803)
	<u>80,260</u>	<u>82,160</u>
	<u>\$ 705,826</u>	<u>\$ 492,470</u>

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)

	<u>Three Months Ended</u> <u>September 30,</u>		<u>Nine Months Ended</u> <u>September 30,</u>	
	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>
Revenues:				
Gain on sale of contracts, net	\$ -	\$ -	\$ -	\$ 8,664
Interest income	25,314	15,835	71,458	36,605
Servicing fees	3,031	4,295	9,864	13,361
Other income	3,918	5,911	11,151	14,674
	<u>32,263</u>	<u>26,041</u>	<u>92,473</u>	<u>73,304</u>
Expenses:				
Employee costs	9,905	9,491	29,352	27,380
General and administrative	4,785	6,050	15,220	14,131
Interest	8,388	6,427	21,800	17,044
Provision for credit losses	7,560	4,190	20,610	4,190
Marketing	2,585	1,400	5,901	4,129
Occupancy	900	1,112	2,651	3,096
Depreciation and amortization	201	223	581	700
	<u>34,324</u>	<u>28,893</u>	<u>96,115</u>	<u>70,670</u>
Income (loss) before income tax benefit	(2,061)	(2,852)	(3,642)	2,634
Income tax benefit	-	-	-	(3,434)
Net income (loss)	<u>\$ (2,061)</u>	<u>\$ (2,852)</u>	<u>\$ (3,642)</u>	<u>\$ 6,068</u>
Earnings (loss) per share:				
Basic	\$ (0.10)	\$ (0.14)	\$ (0.17)	\$ 0.30
Diluted	(0.10)	(0.14)	(0.17)	0.28
Number of shares used in computing earnings (loss) per share:				
Basic	21,345	20,200	21,001	20,226
Diluted	21,345	20,200	21,001	21,711

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

CONSUMER PORTFOLIO SERVICES, INC.
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Nine Months Ended	
	September 30,	
	2004	2003
<i>Cash flows from operating activities:</i>		
Net income (loss)	\$ (3,642)	\$ 6,068
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	581	700
Amortization of deferred financing costs	1,871	2,015
Provision for credit losses	20,610	4,716
NIR (gains) losses recognized	2,650	(6,676)
Loss on sale of furniture and equipment	8	-
Stock-based compensation expense	210	772
Releases of cash from Trusts to Company	17,175	20,227
Initial deposits to Trusts	-	(18,736)
Net deposits to Trusts to increase Credit Enhancement	(2,106)	(19,575)
Decrease in receivables from Trusts and investment in subordinated certificates	25,269	32,690
Changes in assets and liabilities:		
Restricted cash	(46,539)	(24,077)
Purchases of contracts held for sale	-	(182,045)
Amortization and liquidation of contracts held for sale	-	249,660
Servicing fees receivable and other assets	(7,133)	7,786
Accounts payable and accrued expenses	1,161	(2,568)
Tax liabilities, net	181	(6,802)
Net cash provided by operating activities	10,296	64,155
<i>Cash flows from investing activities:</i>		
Purchases of finance receivables held for investment	(374,717)	(92,389)
Amortization of finance receivables held for investment	134,374	1,683
Purchase of furniture and equipment	(838)	(68)
Purchase of subsidiary, net of cash acquired	-	(10,181)
Net cash used in investing activities	(241,181)	(100,955)
<i>Cash flows from financing activities:</i>		
Proceeds from issuance of residual financing debt	44,000	-
Proceeds from issuance of securitization trust debt	363,300	83,125
Proceeds from issuance of senior secured debt	25,000	25,000
Net proceeds from warehouse lines of credit	(17,188)	21,877
Repayment of residual interest financing debt	(16,689)	-
Repayment of securitization trust debt	(130,527)	(68,256)
Repayment of senior secured debt	(15,136)	(24,935)
Repayment of subordinated debt	(20,000)	(34)
Repayment of capital lease obligations	(89)	(80)
Repayment of notes payable	(1,737)	(2,994)
Repayment of related party debt	(16,500)	-
Payment of financing costs	(6,338)	(1,833)
Repurchase of common stock	(25)	(1,195)
Exercise of options and warrants	557	271
Net cash provided by financing activities	208,628	30,946
Decrease in cash	(22,257)	(5,854)
Cash at beginning of period	33,209	32,947
Cash at end of period	\$ 10,952	\$ 27,093
Supplemental disclosure of cash flow information:		
Cash paid (received) during the period for:		
Interest	\$ 19,534	\$ 12,997
Income taxes	(181)	3,369
Supplemental disclosure of non-cash investing and financing activities:		
Stock-based compensation	\$ 35	\$ 772
Conversion of related party debt to common stock	1,000	-
Furniture and equipment acquired through capital leases	480	-

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(1) Summary of Significant Accounting Policies

Description of Business

Consumer Portfolio Services, Inc. (“CPS”) was incorporated in California on March 8, 1991. CPS and its subsidiaries (collectively, the “Company”) specialize primarily in purchasing, selling and servicing retail automobile installment sale contracts (“Contracts” or “finance receivables”) originated by licensed motor vehicle dealers (“Dealers”) located throughout the United States. The Company purchases Contracts with obligors who generally would not be expected to qualify for traditional financing, such as that provided by commercial banks or automobile manufacturers’ captive finance companies.

Acquisition of MFN Financial Corporation

On March 8, 2002, CPS acquired 100% of MFN Financial Corporation, a Delaware corporation (“MFN”) and its subsidiaries, by the merger (the “MFN Merger”) of a direct wholly-owned subsidiary of CPS with and into MFN. MFN thus became a wholly-owned subsidiary of CPS, and CPS thus acquired the assets of MFN, which consisted principally of interests in automobile installment sales finance Contracts and the facilities for originating and servicing such Contracts. The MFN Merger was accounted for as a purchase.

MFN, through its primary operating subsidiary, Mercury Finance Company LLC, was in the business of purchasing automobile installment sales finance Contracts from Dealers, and securitizing and servicing such Contracts. CPS continues to use the assets acquired in the MFN Merger in the automobile finance business, but has disposed of a portion of such assets. MFN has ceased to purchase automobile installment sales finance Contracts, and does not anticipate recommencing such purchasing. In connection with the termination of MFN origination activities and the integration and consolidation of certain activities, the Company has recognized certain liabilities related to the costs to exit these activities and terminate the affected employees of MFN. These activities include service departments such as accounting, finance, human resources, information technology, administration, payroll and executive management. These costs include the following:

	September 30, 2004(1)	Activity	December 31, 2003	Activity	March 8, 2002
	(In thousands)				
Severance payments and consulting contracts.....	\$ -	\$ -	\$ -	\$ 3,215	\$ 3,215
Facilities closures.....	1,358	531	1,889	263	2,152
Termination of contracts, leases, services and other obligations.....	-	-	-	597	597
Acquisition expenses accrued but unpaid.....	-	-	-	250	250
Total liabilities assumed.....	\$ 1,358	\$ 531	\$ 1,889	\$ 4,325	\$ 6,214

(1) The initial accrual amount recorded was \$6.2 million on March 8, 2002 and the remaining accrual recorded in the Unaudited Condensed Consolidated Balance Sheet of the Company is approximately \$1.4 million and \$1.9 million as of September 30, 2004 and December 31, 2003, respectively. The Company believes that this amount provides adequately for anticipated remaining costs related to exiting certain activities of MFN, and that amounts indicated above are reasonably allocated.

Acquisition of TFC Enterprises, Inc.

On May 20, 2003, CPS acquired TFC Enterprises, Inc., a Delaware corporation (“TFC”) and its subsidiaries, by the merger (the “TFC Merger”) of a direct, wholly-owned subsidiary of CPS, with and into TFC. In the TFC Merger, TFC became a wholly-owned subsidiary of CPS. CPS thus acquired the assets of TFC and its subsidiaries, which consisted principally of interests in motor vehicle installment

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

sales finance Contracts, interests in securitized pools of such Contracts, and the facilities for originating and servicing such Contracts. The TFC Merger was accounted for as a purchase.

TFC, through its primary operating subsidiary, "The Finance Company," purchases motor vehicle installment sales finance Contracts from automobile Dealers, and securitizes and services such Contracts. CPS has continued to use the assets acquired in the TFC Merger in the automobile finance business.

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

	September 30, 2004(1)	Activity	December 31, 2003
	(In thousands)		
Severance payments and consulting contracts.....	\$ 1,782	\$ 544	\$ 2,326
Facilities closures.....	890	341	1,231
Other obligations.....	49	185	234
Total liabilities assumed.....	\$ 2,721	\$ 1,070	\$ 3,791

(1) The initial accrual amount recorded was \$4.5 million on May 20, 2003 and the remaining accrual recorded in the Unaudited Condensed Consolidated Balance Sheet of the Company is approximately \$2.7 million and \$3.8 million as of September 30, 2004 and December 31, 2003, respectively. The Company believes that this amount provides adequately for anticipated remaining costs related to exiting certain activities of TFC, and that amounts indicated above are reasonably allocated.

At the closing of the TFC Merger, each outstanding share of common stock of TFC became a right to receive \$1.87 per share in cash. The total merger consideration paid to stockholders of TFC was approximately \$21.6 million. The recipients of the total merger consideration had no material relationship with CPS, its directors, its officers or any associates of such directors or officers, to the best of CPS's knowledge. The merger consideration was paid with existing cash of CPS. The aggregate purchase price, including expenses related to the transaction, was approximately \$23.7 million.

The Company's Unaudited Condensed Consolidated Balance Sheet and Unaudited Condensed Consolidated Statements of Operations as of and for the three and nine months ended September 30, 2004, include the balance sheet accounts of TFC as of September 30, 2004 and the results of its operations subsequent to May 20, 2003, the merger date. The Company has recorded certain purchase accounting adjustments on its Unaudited Condensed Consolidated Balance Sheet, which are estimates based on available information.

The following table summarizes the recorded amounts of the assets acquired and liabilities assumed at the date of acquisition.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

	<u>May 20, 2003</u>
	<u>(In thousands)</u>
Cash.....	\$ 13,545
Restricted cash.....	17,723
Finance receivables, net.....	125,108
Other assets.....	502
Total assets acquired.....	<u>156,878</u>
Securitization trust debt.....	115,597
Subordinated debt.....	6,321
Capital lease obligations.....	17
Accounts payable and other liabilities.....	11,217
Total liabilities assumed.....	<u>133,152</u>
Purchase price.....	<u>\$ 23,726</u>

Pro Forma Results of Operations

Selected unaudited pro forma combined results of operations for the three- and nine-month periods ended September 30, 2003, assuming the TFC Merger occurred on January 1, 2003, are as follows:

	<u>Three Months Ended</u>		<u>Nine Months Ended</u>
	<u>September 30,</u>		<u>September 30,</u>
	<u>2003</u>		<u>2003</u>
	<u>(In thousands)</u>		
Total revenue.....	\$ 25,487	\$	78,413
Net earnings (loss).....	(2,852)	\$	6,497
Basic net earnings (loss) per share.....	(0.14)	\$	0.32
Diluted net earnings (loss) per share.....	(0.14)	\$	0.30

Acquisition of Receivables and Other Assets from SeaWest Financial Corporation

The Company on April 2, 2004 acquired automotive finance receivables and other assets (the “SeaWest Asset Acquisition”) of SeaWest Financial Corporation (“SeaWest”). The aggregate purchase price was approximately \$63.2 million, which was funded with the proceeds of an acquisition financing facility and existing cash. The receivables were purchased at a discount to par and such discount has been accounted for as a non-accretable discount. The other assets included a \$2.8 million note to an affiliate of SeaWest and certain furniture and equipment. In addition, the Company has been appointed the successor servicer on three separate term securitization transactions originally sponsored by SeaWest (the “SeaWest Third Party Portfolio”).

Basis of Presentation

The unaudited Condensed Consolidated Financial Statements of the Company have been prepared in conformity with accounting principles generally accepted in the United States of America, with the instructions to Form 10-Q and with Article 10 of Regulation S-X of the Securities and Exchange Commission, and include all adjustments that are, in the opinion of management, necessary for a fair presentation of the results for the interim periods presented. All such adjustments are, in the opinion of management, of a normal recurring nature. In addition, certain items in prior period financial statements have been reclassified for comparability to current period presentation. Results for the three- and nine-month periods ended September 30, 2004 are not necessarily indicative of the operating results to be expected for the full year.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted from these Unaudited Condensed Consolidated Financial Statements. These Unaudited Condensed Consolidated Financial Statements should be read in conjunction with the

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Consolidated Financial Statements and Notes to Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2003.

Recent Developments

In July 2003, the Company agreed with the other parties to its continuous or "warehouse" securitization facilities to amend the terms of such facilities. The effect of the amendments was to cause use of those facilities to be treated for financial accounting purposes as borrowings secured by pledged Contracts, rather than as sales of such Contracts.

In addition, the Company announced in August 2003 that it would structure its future term securitization transactions so that they would be treated for financial accounting purposes as borrowings secured by receivables, rather than as sales of receivables. The new structure for the warehouse facilities described in the preceding paragraph and the change in structure of the Company's term securitizations has affected and will affect the way in which the transactions are reported. The major effects are these: (i) the finance receivables are shown as assets of the Company on its balance sheet; (ii) the debt issued in the transactions is shown as indebtedness of the Company on its balance sheet; (iii) cash deposited to enhance the credit of the securitization transactions is shown as "restricted cash" on the Company's balance sheet; (iv) cash collected from borrowers and other sources related to the receivables prior to making the required payments under the Securitization Agreements is also shown as "Restricted cash" on the Company's balance sheet; (v) the servicing fee that the Company receives in connection with such receivables is recorded as a portion of the interest earned on such receivables in the Company's statements of operations; (vi) the Company has initially and periodically recorded as expense a provision for credit losses on the receivables in the Company's statements of operations; and (vii) the portion of scheduled payments on the receivables representing interest is recorded as revenue as earned in the Company's statements of operations.

These changes collectively represent a deferral of revenue and acceleration of expenses, and thus a more conservative approach to accounting for the Company's operations. The changes initially have resulted in the Company reporting lower earnings than it would have reported if it had continued structuring its securitizations to require recognition of gain on sale.

Treatment of Securitizations

Gain on sale may be recognized on the disposition of Contracts either outright or in securitization transactions. In those securitization transactions that were sales for financial accounting purposes, the Company, or a wholly-owned consolidated subsidiary of the Company, retained a residual interest in the Contracts that were sold to a wholly-owned unconsolidated special purpose subsidiary. The Company's securitization transactions include "term" securitizations (the purchaser holds the Contracts for substantially their entire term) and "continuous" or "warehouse" securitizations (which finance the acquisition of the Contracts for future sale into term securitizations).

As of September 30, 2004 and December 31, 2003, the line item "Residual interest in securitizations" on the Company's Unaudited Condensed Consolidated Balance Sheet represents the residual interests in certain term securitizations but no residual interest in warehouse securitizations, because the Company's warehouse securitizations were restructured in July 2003 as secured financings. Term securitizations of receivables purchased under the CPS programs subsequent to July 2003 were also structured as secured financings. The warehouse securitizations are accordingly reflected in the line items "Finance receivables" and "Warehouse lines of credit" on the Company's Unaudited Condensed Consolidated Balance Sheet, and the term securitizations are reflected in the line items "Finance receivables" and "Securitization trust debt." The line item "Residual interest in securitizations" represents the discounted sum of expected future releases from securitization trusts that were structured as sales prior to July 2003. Accordingly, the valuation of the residual is heavily dependent on estimates of future performance.

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The Company's securitization structure is generally as follows:

The Company sells Contracts it acquires to a wholly-owned Special Purpose Subsidiary ("SPS"), which has been established for the limited purpose of buying and reselling the Company's Contracts. The SPS then transfers the same Contracts to another entity, typically a statutory trust ("Trust"). The Trust issues interest-bearing asset-backed securities (the "Notes"), generally in a principal amount equal to the aggregate principal balance of the Contracts. The Company typically sells these Contracts to the Trust at face value and without recourse, except that representations and warranties similar to those provided by the Dealers to the Company are provided by the Company to the Trust. One or more investors purchase the Notes issued by the Trust; the proceeds from the sale of the Notes are then used to purchase the Contracts from the Company. The Company may retain or sell subordinated Notes issued by the Trust. The Company purchases a financial guaranty insurance policy, guaranteeing timely payment of principal and interest on the senior Notes, from an insurance company (a "Note Insurer"). In addition, the Company provides "Credit Enhancement" for the benefit of the Note Insurer and the investors in the form of an initial cash deposit to a bank account (a "Spread Account") held by the Trust; in the form of overcollateralization of the Notes, where the principal balance of the Notes issued is less than the principal balance of the Contracts; in the form of subordinated Notes; or some combination of such Credit Enhancements. The agreements governing the securitization transactions (collectively referred to as the "Securitization Agreements") require that the initial level of Credit Enhancement be supplemented by a portion of collections from the Contracts until the level of Credit Enhancement reaches specified levels, and then maintained at those levels. The specified levels are generally computed as a percentage of the remaining unpaid principal amount under the related Contracts. The specified levels at which the Credit Enhancements are to be maintained will vary depending on the performance of the portfolios of Contracts held by the Trusts and on other conditions, and may also be varied by agreement among the Company, the SPS, the Note Insurers and the trustee. Such levels have increased and decreased from time to time based on performance of the portfolios, and have also varied by Securitization Agreement. The Securitization Agreements generally grant the Company the option to repurchase the sold Contracts from the Trust when the aggregate outstanding balance has amortized to a specified percentage of the initial aggregate balance.

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

The Company's warehouse securitization structures are similar to the above, except that (i) the SPS that purchases the Contracts pledges the Contracts to secure promissory notes that it issues, (ii) the promissory notes are in an aggregate principal amount of not more than 73.0% to 73.5% of the aggregate principal balance of the Contracts (that is, at least 26.5% overcollateralization), and (iii) no increase in the required amount of Credit Enhancement is contemplated unless certain portfolio performance tests are breached. During the quarter ended September 30, 2003, the warehouse securitizations related to the CPS programs were amended to provide for the transactions to be reflected as secured financings for financial accounting purposes. The Contracts held by the warehouse SPS and the promissory notes that it issues are therefore included in the Company's Unaudited Condensed Consolidated Financial Statements as of September 30, 2004 and December 31, 2003 as assets and liabilities, respectively.

Upon each sale of Contracts in a securitization structured as a secured financing, whether a term securitization or a continuous securitization, the Company retains on its Unaudited Condensed Consolidated Balance Sheet the Contracts securitized as assets and records the Notes issued in the transaction as indebtedness of the Company.

Under the prior securitizations structured as sales for financial accounting purposes, the Company removed from its Unaudited Condensed Consolidated Balance Sheet the Contracts sold and added to its Unaudited Condensed Consolidated Balance Sheet (i) the cash received and (ii) the estimated fair value of

CONSUMER PORTFOLIO SERVICES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

the ownership interest that the Company retains in Contracts sold in the securitization. That retained or residual interest (the "Residual") consists of (a) the cash held in the Spread Account, if any, (b) overcollateralization, if any, (c) subordinated Notes retained, if any, and (d) receivables from Trust, which include the net interest receivables ("NIRs"). NIRs represent the estimated discounted cash flows to be received from the Trust in the future, net of principal and interest payable with respect to the Notes, and certain expenses. The excess of the cash received and the assets retained by the Company over the carrying value of the Contracts sold, less transaction costs, equals the net gain on sale of Contracts recorded by the Company. Until the maturity of these transactions, the Company's Unaudited Condensed Consolidated Balance Sheet will reflect securitization transactions structured both as sales and as secured financings.

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

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

If the amount of cash required for payment of fees, interest on the Notes and principal of the Notes exceeds the amount collected during the collection period, the shortfall is withdrawn from the Spread Account, if any. If the cash collected during the period exceeds the amount necessary for the above allocations, and there is no shortfall in the related Spread Account, the excess is released to the Company, or in certain cases is transferred to other Spread Accounts that may be below their required levels. If the Spread Account balance is not at the required credit enhancement level, then the excess cash collected is retained in the Spread Account until the specified level is achieved. Although Spread Account balances are held by the Trusts on behalf of the Company's SPS as the owner of the Residuals (in the case of securitization transactions structured as sales for financial accounting purposes) or as the owner of the Trusts (in the case of securitization transactions structured as secured financings for financial accounting purposes), the cash in the Spread Accounts is restricted from use by the Company. Cash held in the various Spread Accounts is invested in high quality, liquid investment securities, as specified in the Securitization Agreements. The interest rate payable on the Contracts is significantly greater than the interest rate on the Notes. As a result, the Residuals described above are a significant asset of the Company. In determining the value of the Residuals, the Company must estimate the future rates of prepayments, delinquencies, defaults, default loss severity, and recovery rates, as all of these factors affect the amount and timing of the estimated cash flows. The Company estimates prepayments by evaluating historical prepayment performance of comparable Contracts. As of September 30, 2004, the Company has used prepayment estimates of approximately 19.4% to 24.6% cumulatively over the lives of

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

the related Contracts. The Company estimates defaults and default loss severity using available historical loss data for comparable Contracts and the specific characteristics of the Contracts purchased by the Company. The Company estimates recovery rates of previously charged off receivables using available historical recovery data and projected future recovery levels. In valuing the Residuals as of September 30, 2004, the Company estimates that charge-offs as a percentage of the original principal balance will approximate 15.1% to 24.0% cumulatively over the lives of the related Contracts, with recovery rates approximating 2.6% to 5.6% of the original principal balance.

Following a securitization that is structured as a sale for financial accounting purposes, interest income is generally recognized on the balance of the Residuals at the same rate as used for calculating the present value of the NIRs, which is equal to 14% per annum. In addition, the Company will recognize additional revenue from the Residuals if the actual performance of the Contracts is better than the original estimate. If the actual performance of the Contracts were worse than the original estimate, then an impairment loss would be required to reduce the carrying value of the Residuals. In the quarter ended September 30, 2004, the Company recorded an impairment loss of \$2.6 million related to the Company's analysis and estimate of the expected ultimate performance of the Company's previously securitized pools that are held by non-consolidated subsidiaries. In a securitization structured as a secured financing for financial accounting purposes, interest income is recognized when accrued under the terms of the related Contracts and, therefore, presents less potential for fluctuations in performance when compared to the approach used in a transaction structured as a sale for financial accounting purposes.

In all the Company's term securitizations, whether treated as secured financings or as sales, the Company has transferred the receivables (through a subsidiary) to the securitization Trust. The difference between the two structures is that in securitizations that are treated as secured financings the Company reports the assets and liabilities of the securitization Trust on its Unaudited Condensed Consolidated Balance Sheet. Under both structures the Noteholders and the related securitization Trusts have no recourse to the Company for failure of the Contract obligors to make payments on a timely basis. The Company's Residuals, however, are subordinate to the Notes until the Noteholders are fully paid, and the Company is therefore at risk to that extent.

Other Income

Other income consists primarily of recoveries on certain previously charged off Contracts and state sales tax refunds relating to previously charged-off loans.

Stock Based Compensation

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

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

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	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003	2004	2003
	<i>(In thousands, except per share data)</i>			
Net income (loss), as reported.....	\$ (2,061)	\$ (2,852)	\$ (3,642)	\$ 6,068
Stock-based employee compensation expense, fair value method, net of tax.....	(231)	(214)	(626)	(639)
Previously recorded stock-based employee compensation expense, intrinsic value method, net of tax.....	36	189	122	448
Pro forma net income (loss).....	<u>\$ (2,256)</u>	<u>\$ (2,877)</u>	<u>\$ (4,146)</u>	<u>\$ 5,877</u>
Net income (loss) per share.....				
Basic, as reported.....	\$ (0.10)	\$ (0.14)	\$ (0.17)	\$ 0.30
Diluted, as reported (1).....	\$ (0.10)	\$ (0.14)	\$ (0.17)	\$ 0.28
Pro forma Basic.....	\$ (0.11)	\$ (0.14)	\$ (0.20)	\$ 0.29
Pro forma Diluted (1).....	\$ (0.11)	\$ (0.14)	\$ (0.20)	\$ 0.27

(1) The assumed conversion of certain subordinated debt during the nine-month periods ended September 30, 2003, resulted in an increase to income for purposes of the diluted earnings per share calculation of \$54,979.

Pro forma net income (loss) and income (loss) per share reflect only options granted in the years ended December 31, 1996 to September 30, 2004. Therefore, the full effect of calculating compensation cost for stock options under SFAS No. 123 is not reflected in the pro forma amounts presented above, as compensation expense for options granted prior to 1996 is not considered.

Purchases of Company Stock

During the nine-month periods ended September 30, 2004 and 2003, the Company purchased 6,738 and 548,426 shares, respectively, of its common stock at an average price of \$3.75 and \$2.18, respectively.

New Accounting Pronouncements

In December 2003, the FASB issued FASB Interpretation No. 46 (revised December 2003, FIN 46R), *Consolidation of Variable Interest Entities*, which addresses how a business enterprise should evaluate whether it has a controlling financial interest in an entity through means other than voting rights and accordingly should consolidate the entity. FIN 46R replaces FASB Interpretation No. 46, *Consolidation of Variable Interest Entities*, which was issued in January 2003. The Company is required to apply FIN 46R to variable interests in Variable Interest Entities (“VIEs”) created after December 31, 2003. For variable interests in VIEs created before January 1, 2004, the Interpretation will be applied beginning on January 1, 2005. For any VIEs that must be consolidated under FIN 46R that were created before January 1, 2004, the assets, liabilities and noncontrolling interests of the VIE initially is measured at their carrying amounts with any difference between the net amount added to the balance sheet and any previously recognized interest being recognized as the cumulative effect of an accounting change. If determining the carrying amounts is not practicable, fair value at the date FIN 46R first applies may be used. Certain of the Company’s subsidiaries are qualifying special purpose entities formed in connection with off-balance sheet securitizations and are not subject to the requirements of FIN 46R. The Company’s subsidiaries that are considered VIEs subject to the requirements of FIN 46R consist of Trusts related to the Company’s on-balance sheet securitizations, which are consolidated and in the Company’s consolidated financial statements. The adoption of FIN 46R did not have a material effect on the Company.

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(2) Finance Receivables

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

	September 30, 2004	December 31, 2003
	(In thousands)	
Finance Receivables		
Automobile		
Simple Interest.....	\$ 449,729	\$ 178,679
Pre-compute or "Rule of 78's", net of unearned interest.....	97,412	133,339
Finance Receivables, net of unearned interest.....	547,141	312,018
Less: Unearned acquisition fees and discounts.....	(22,191)	(9,940)
Finance Receivables.....	<u>\$ 524,950</u>	<u>\$ 302,078</u>

The following table presents the contractual maturities of Finance Receivables, net of unearned income as of September 30, 2004:

	Amount	%
	(Dollars in thousands)	
Due in 2004.....	\$ 2,283	0.42%
Due in 2005.....	18,791	3.43%
Due in 2006.....	36,286	6.63%
Due in 2007.....	53,029	9.69%
Due in 2008.....	136,087	24.87%
Due thereafter.....	300,665	54.95%
Total.....	<u>\$ 547,141</u>	<u>100.00%</u>

The following table presents a summary of the activity for the allowance for finance credit losses for the nine-month periods ended September 30, 2004 and 2003:

	September 30, 2004	September 30, 2003
	(In thousands)	
Balance at beginning of period.....	\$ 35,889	\$ 25,828
Addition to allowance for credit losses from acquisitions.....	-	24,271
Provision for credit losses.....	20,610	4,716
Net charge offs.....	(17,471)	(16,798)
Balance at end of period.....	<u>\$ 39,028</u>	<u>\$ 38,017</u>

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(3) Residual Interest in Securitizations

The following table presents the components of the residual interest in securitizations:

	<u>September 30,</u> <u>2004</u>	<u>December 31,</u> <u>2003</u>
	(In thousands)	
Cash, commercial paper, United States government securities and other qualifying investments (Spread Accounts).....	\$ 26,394	\$ 35,693
Receivables from Trusts (NIRs).....	15,500	20,959
Overcollateralization.....	22,795	38,548
Investment in subordinated certificates.....	4,025	16,502
Residual interest in securitizations.....	<u>\$ 68,714</u>	<u>\$ 111,702</u>

The following table presents estimated remaining undiscounted credit losses included in the estimated fair value of the residual interest in securitizations as a percentage of the Company's non-consolidated servicing portfolio subject to recourse provisions:

	<u>September 30,</u> <u>2004</u>	<u>December 31,</u> <u>2003</u>
	(Dollars in thousands)	
Undiscounted estimated credit losses.....	\$ 22,372	\$ 47,935
Managed portfolio held by non-consolidated subsidiaries.....	276,202	425,534
Undiscounted estimated credit losses as percentage of managed portfolio held by non-consolidated subsidiary	8.1%	11.3%

(4) Residual Interest Financing

On March 16, 2004, a special-purpose subsidiary of CPS issued \$44 million of asset-backed 10% notes. The notes, issued by CPS Auto Receivables Trust 2004-R, are rated BBB by Standard & Poor's and have a final maturity date of October 16, 2009. The notes are secured by the Company's residual interest in four securitizations sponsored by CPS, two securitizations sponsored by MFN, and two securitization transactions sponsored by TFC. The notes are non-recourse obligations of the Company and will be repaid solely from the cash distributions on the retained interests securing the notes.

(5) Securitization Trust Debt

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

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Series	Issue Date	Initial Principal	Outstanding Principal at September 30, 2004	Outstanding Principal at December 31, 2003	Weighted Average Coupon as of September 30, 2004
(Dollars in thousands)					
CPS 2004-C	September 30, 2004	\$ 91,000	\$ 91,000	\$ N/A	2.74%
CPS 2004-B	August 2, 2004	96,370	90,949	N/A	3.08%
PCR 2004-1	June 24, 2004	76,257	63,174	N/A	3.11%
CPS 2004-A	May 5, 2004	76,347	72,353	N/A	3.19%
CPS 2003-D	December 16, 2003	71,250	56,695	71,250	2.91%
CPS 2003-C	September 30, 2003	83,125	60,172	77,928	2.85%
TFC 2003-1	May 20, 2003	52,365	21,715	37,114	2.69%
TFC 2002-2	October 9, 2002	62,589	11,995	25,436	2.95%
TFC 2002-1	March 19, 2002	64,552	4,090	12,403	4.23%
MFN 2001-A	June 28, 2001	301,000	5,748	20,987	5.07%
		<u>\$ 974,855</u>	<u>\$ 477,891</u>	<u>\$ 245,118</u>	

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

The terms of the various Securitization Agreements related to the issuance of the securitization trust debt require that certain delinquency and credit loss criteria be met with respect to the collateral pool, and require that the Company maintain a minimum net worth and meet other financial tests. As of September 30, 2004, the Company was not in default of any provisions of the agreements as amended, except one related to the minimum cash balance on the closing date of a term securitization transaction. The controlling party has waived this covenant breach. The Company is responsible for the administration and collection of the Contracts. The Securitization Agreements also require certain funds be held in restricted cash accounts to provide additional collateral for the borrowings or to be applied to make payments on the securitization trust debt. As of September 30, 2004, restricted cash under the various agreements totaled approximately \$108.0 million. Interest expense on the securitization trust debt is composed of the stated rate of interest plus amortization of additional costs of borrowing. Additional costs of borrowing include facility fees, insurance and deferred financing costs. Deferred financing costs related to the securitization trust debt are amortized in proportion to the principal distributed to the noteholders. Accordingly, the effective cost of borrowing of the securitization trust debt is greater than the weighted average coupon appearing in the table above.

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

(6) Senior Secured Debt

On February 3, 2003, the Company borrowed \$25.0 million from Levine Leichtman Capital Partners II, L.P. ("LLCP"), net of fees and expenses of \$1.05 million. The indebtedness, represented by the "Term D Note," was originally due in April 2003, with Company options to extend the maturity to May 2003 and

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January 2004, upon payment of successive extension fees of \$125,000. The Company paid the fees to extend the maturity to January 2004.

The Company had previously borrowed other amounts from LLC in the form of the "Term B Note" and the "Term C Note." The Company repaid in full the Term C Note on January 29, 2004 and repaid \$10.0 million of the Term D Note on January 15, 2004. In addition, on January 29, 2004 the maturities of the Term B Note and the remaining \$15.0 million of the Term D Note were extended to December 15, 2005, and the interest rates applicable to both notes were decreased to 11.75% per annum, from 14.50% and 12.00%, respectively. The Company paid LLC fees equal to \$921,000 for these amendments, which were deferred and are amortized over the remaining life of the notes. As of September 30, 2004, the outstanding principal balances of the Term B Note and the Term D Note were \$19.8 million and \$15.0 million, respectively.

On May 28, 2004 and June 25, 2004, the Company borrowed \$15 million and \$10 million, respectively, from LLC. The indebtedness, represented by the "Term E Note," and the "Term F Note," respectively, bears interest at 11.75% per annum. Both the Term E Note and the Term F Note mature two years from their respective funding dates. As of September 30, 2004, the outstanding principal balances of the Term E Note and the Term F Note were \$15.0 million and \$10.0 million, respectively.

The Senior Secured Debt is secured by all of the assets of the Company.

(7) Net Gain on Sale of Contracts

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003	2004	2003
	(In thousands)			
Gain (loss) recognized on sale.....	\$ -	\$ -	\$ -	\$ 6,676
Deferred acquisition fees and discounts.....	-	-	-	4,590
Expenses related to sales.....	-	-	-	(2,076)
Provision for credit losses.....	-	-	-	(526)
Net gain on sale of Contracts.....	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 8,664</u>

No gain on sale was recorded in the three-month periods ended September 30, 2004 and 2003 and the nine-month period ended September 30, 2004, due to the July 2003 decision to structure future securitizations as secured financings, rather than as sales.

(8) Interest Income

The following table presents the components of interest income:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003	2004	2003
	(In thousands)			
Interest on finance receivables.....	27,695	11,731	68,405	23,841
Residual interest income (expense), net of impairment loss.....	(2,650)	3,682	1,984	12,070
Other interest income.....	269	422	1,069	694
Net interest income.....	<u>25,314</u>	<u>15,835</u>	<u>71,458</u>	<u>36,605</u>

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(9) Earnings (Loss) Per Share

Diluted earnings (loss) per share for the three-month and nine-month periods ended September 30, 2004 and 2003 were calculated using the weighted average number of shares outstanding for the related period. The following table reconciles the number of shares used in the computations of basic and diluted earnings (loss) per share for the three-month and nine-month periods ended September 30, 2004 and 2003:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003	2004	2003
	(In thousands)			
Weighted average number of common shares outstanding during the period used to compute basic earnings (loss) per share.....	21,345	20,200	21,001	20,226
Incremental common shares attributable to exercise of outstanding options and warrants.....	-	-	-	1,152
Incremental common shares attributable to convertible debt.....	-	-	-	333
Weighted average number of common shares used to compute diluted earnings per share.....	21,345	20,200	21,001	21,711

The assumed conversion of certain subordinated debt during the nine-month period ended September 30, 2003, resulted in an increase to income for purposes of the diluted earnings per share calculation of \$55,000, representing interest attributable to convertible debt that would not have been incurred if the convertible debt had been converted. Diluted net earnings for purposes of the diluted earnings per share calculation totaled \$6.1 million for the nine months ended September 30, 2003.

If the anti-dilutive effects of common stock equivalents were considered, additional shares included in the diluted earnings (loss) per share calculation for the three-month and nine-month periods ended September 30, 2004 would have included an additional 1.9 million and 1.8 million shares, respectively, attributable to the exercise of outstanding options and warrants. Similarly, additional shares included in the diluted earnings per share calculation for the three-month and nine-month periods ended September 30, 2003 would have included an additional 2.8 million and 746,000 shares, respectively, attributable to the conversion of certain subordinated debt and the exercise of outstanding options and warrants.

(10) Income Taxes

As of December 31, 2003, the Company had a net deferred tax asset of \$411,000, which included a valuation allowance of \$37.4 million against certain deferred tax assets of \$44.6 million. Tax liabilities, net, at September 30, 2004 and December 31, 2003 were \$2.9 million and \$2.8 million, respectively. The Company increased its valuation allowance by the income tax benefit for the period to result in no net income tax provision for the three- and nine-month periods ended September 30, 2004. The tax benefit for the nine months ended September 30, 2003 is primarily the result of the resolution of certain Internal Revenue Service examinations of previously filed MFN tax returns, resulting in a tax benefit of \$4.9 million, and other state tax matters. The Company has evaluated its deferred tax assets and believes that it is more likely than not that certain deferred tax assets will not be realized due to limitations imposed by the Internal Revenue Code and expected future taxable income.

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(11) Liquidity

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

Contracts are purchased from Dealers for a cash price generally approximating their principal amount, and generate cash flow over a period of years. As a result, the Company has been dependent on warehouse credit facilities to purchase Contracts, and on the availability of cash from outside sources in order to finance its continuing operations, as well as to fund the portion of Contract purchase prices not financed under warehouse credit facilities. As of September 30, 2004, the Company had \$225 million in warehouse credit capacity, in the form of a \$125 million facility and a \$100 million facility. Both warehouse facilities provide funding for Contracts purchased under the CPS Programs. A third facility in the amount of \$75 million, which the Company also utilized to fund Contracts under the CPS Programs, expired on February 21, 2004. A fourth facility in the amount of \$25 million, which the Company utilized to fund Contracts under the TFC Programs, expired on June 24, 2004.

The Company's primary means of ensuring that its cash demands do not exceed its cash resources is to match its levels of Contract purchases to its availability of cash. The Company's ability to adjust the quantity of Contracts that it purchases and securitizes will be subject to general competitive conditions and the continued availability of warehouse credit facilities. There can be no assurance that the desired level of Contract acquisition can be maintained or increased. Obtaining releases of cash from the Trusts and their related Spread Accounts is dependent on collections from the related Trusts generating sufficient cash to maintain the Spread Accounts in excess of their respective requisite levels. There can be no assurance that collections from the related Trusts will continue to generate sufficient cash.

Certain of the Company's securitization transactions and the warehouse credit facilities contain various covenants requiring certain minimum financial ratios and results. As a result of amendments to the related Securitization Agreements executed during the first nine months of 2004, the Company was in compliance with all of these covenants as of September 30, 2004, except one related to the minimum cash balance on the closing date of a term securitization transaction. The controlling party has waived this covenant breach.

(12) Legal Proceedings

The information provided under the caption "Legal Proceedings" in the Company's Annual Report of Form 10-K for the year ended December 31, 2003 is incorporated herein by reference. In addition, the reader should be aware of the following:

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On June 2, 2004, Delmar Coleman filed a lawsuit in the circuit court of Tuscaloosa, Alabama, making allegations similar to those that were asserted in the *Lang* case, and seeking damages in an unspecified amount, on behalf of a purported nationwide class. (The *Lang* case has been settled on the terms disclosed in the Annual Report, and related to alleged defects in the notices given with respect to repossessed vehicles.) CPS believes that it has one or more defenses to each of the claims made in this lawsuit, and intends to defend the matter vigorously.

On June 15, 2004, Keywana Booker filed a lawsuit in the federal district court of Atlanta, Georgia, alleging violations of the Fair Debt Collection Practices Act, and seeking damages in an unspecified amount on behalf of a purported class of Georgia residents. The Company has reached an agreement in principle to settle the *Booker* lawsuit payment of an immaterial amount.

On July 14, 2004, Jeremy Henry filed a lawsuit in the superior court of San Diego, California, alleging that he, and a purported California class, were harmed by alleged defects in post-repossession notices. The notice in question is a form that was used by TFC prior to TFC's having been acquired by CPS, and for a short time thereafter. CPS believes that it has one or more defenses to each of the claims made in the lawsuit, and intends to defend this matter vigorously.

The Company is routinely involved in various legal proceedings resulting from its consumer finance activities and practices, both continuing and discontinued. The Company believes that there are substantive legal defenses to such claims, and intends to defend them vigorously. There can be no assurance, however, as to the outcome.

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

General

Consumer Portfolio Services, Inc. ("CPS," and together with its subsidiaries, the "Company") is a consumer finance company specializing in purchasing, selling and servicing retail automobile installment purchase contracts ("Contracts") originated by licensed motor vehicle dealers ("Dealers") in the sale of new and used automobiles, light trucks and passenger vans. Through its purchases, the Company provides indirect financing to Dealer customers with limited credit histories, low incomes or past credit problems ("Sub-Prime Customers"). The Company serves as an alternative source of financing for Dealers, allowing sales to customers who otherwise might not be able to obtain financing. The Company does not lend money directly to consumers. Rather, it purchases installment Contracts from Dealers.

CPS was incorporated and began its operations in 1991. In March 2002, CPS acquired by merger (the "MFN Merger") MFN Financial Corp. and its subsidiaries. In May 2003, CPS acquired by merger (the "TFC Merger") TFC Enterprises Inc. and its subsidiaries. Both MFN Financial Corp and TFC Enterprises Inc., through their respective subsidiaries, were engaged in businesses substantially similar to that of CPS, and in each merger CPS acquired a portfolio of receivables that had been held by the acquired company. Each merger was accounted for as a purchase. The indirect financing programs of subsidiaries of TFC Enterprises, Inc. were directed principally to members of the United States armed forces. The Company has continued to offer such financing programs (the "TFC Programs") subsequent to the TFC merger, in addition to its other financing programs (the "CPS Programs").

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

Securitization

Generally

Throughout the periods for which information is presented in this report, the Company has purchased Contracts with the intention of repackaging them in securitizations. All such securitizations have involved identification of specific Contracts, sale of those Contracts (and associated rights) to a special purpose subsidiary of the Company, and issuance of asset-backed securities to fund the transactions. Depending on the structure of the securitization, the transaction may be properly accounted for as a sale of the Contracts, or as a secured financing.

When the transaction is structured as a secured financing, the subsidiary is consolidated with the Company. Accordingly, the sold Contracts and the related securitization trust debt appear as assets and liabilities, respectively, of the Company on its Unaudited Condensed Consolidated Balance Sheet. The Company then periodically (i) recognizes interest and fee income on the receivables (ii) recognizes interest expense on the securities issued in the securitization, and (iii) records as expense a provision for credit losses on the receivables.

When structured as a sale, the subsidiary is not consolidated with the Company. Accordingly, the securitization removes the sold Contracts from the Company's Unaudited Condensed Consolidated Balance Sheet, the asset-backed securities (debt of the non-consolidated subsidiary) do not appear as debt of the Company, and the Company shows as an asset a retained residual interest in the sold Contracts. The residual interest represents the discounted value of what the Company expects will be the excess of future collections on the Contracts over principal and interest due on the asset-backed securities. That residual

interest appears on the Company's balance sheet as "Residual interest in securitizations," and the determination of its value is dependent on estimates of the future performance of the sold Contracts.

Change in Policy

In August 2003, the Company announced that it would structure its future securitization transactions as secured financings for financial accounting purposes. Its five subsequent term securitizations of finance receivables have been so structured. Prior to August 2003, the Company had structured its term securitization transactions related to the CPS Programs as sales for financial accounting purposes. In the MFN Merger and in the TFC Merger the Company acquired finance receivables that had been previously securitized in term securitization transactions that were reflected as secured financings. As of September 30, 2004, the Company's Unaudited Condensed Consolidated Balance Sheet included net finance receivables of approximately \$61.0 million and securitization trust debt of \$81.5 million related to finance receivables acquired in the two mergers and the SeaWest Asset Acquisition, out of totals of net finance receivables of approximately \$485.9 million and securitization trust debt of approximately \$477.9 million.

Credit Risk Retained

Whether a securitization is treated as a secured financing or as a sale for financial accounting purposes, the related special purpose subsidiary may be unable to release excess cash to the Company if the credit performance of the securitized Contracts falls short of pre-determined standards. Such releases represent a material portion of the cash that the Company uses to fund its operations. An unexpected deterioration in the performance of securitized Contracts could therefore have a material adverse effect on both the Company's liquidity and its results of operations, regardless of whether such Contracts are treated as having been sold or as having been financed. For estimation of the magnitude of such risk, it may be appropriate to look to the size of the Company's "managed portfolio," which represents both financed and sold Contracts as to which such credit risk is retained. The Company's managed portfolio as of September 30, 2004 was approximately \$898.3 million (this amount includes \$68.2 million related to the SeaWest Third Party Portfolio on which the Company earns only servicing fees and has no credit risk).

Results of Operations

Acquisition

The Company's Unaudited Condensed Consolidated Balance Sheet and Unaudited Condensed Consolidated Statements of Operations as of and for the three and nine months ended September 30, 2004 and 2003, include the results of operations of TFC Enterprises, Inc. for the period subsequent to May 20, 2003, which is the date on which the Company acquired that corporation and its subsidiaries in the TFC Merger. See Note 1 of Notes to Unaudited Condensed Consolidated Financial Statements, Acquisition of TFC Enterprises, Inc.

Effects of Change in Securitization Structure

The Company's decision to structure securitization transactions as borrowings secured by receivables for financial accounting purposes, rather than as sales of receivables, has affected and will affect the way in which the transactions are reported. The major effects are these: (i) the finance receivables are shown as assets of the Company on its balance sheet; (ii) the debt issued in the transactions is shown as indebtedness of the Company; (iii) cash deposited to enhance the credit of the securitization transactions ("Spread Accounts") is shown as "Restricted cash" on the Company's balance sheet; (iv) cash collected from borrowers and other sources related to the receivables prior to making the required payments under the Securitization Agreements is also shown as "Restricted cash" on the Company's balance sheet; (v) the servicing fee that the Company receives in connection with such receivables is recorded as a portion of the interest earned on such receivables in the Company's statements of operations; (vi) the Company has

initially and periodically recorded as expense a provision for credit losses on the receivables in the Company's statements of operations; and (vii) the portion of scheduled payments on the receivables representing interest is recorded as revenue as earned in the Company's statements of operations.

These changes collectively represent a deferral of revenue and acceleration of expenses, and thus a more conservative approach to accounting for the Company's operations. The changes initially have resulted, and may continue to result, in the Company's reporting lower earnings than it would have reported if it had continued structuring its securitizations to require recognition of gain on sale. It should also be noted that growth in the Company's portfolio of receivables in excess of current expectations would result in an increase in expenses in the form of provision for credit losses, and would have a negative effect on net earnings. The Company's cash availability and cash requirements have been unaffected by the change in structure.

The Company's first five term securitizations of Contracts originated under the CPS Programs structured as secured financings closed in September 2003, December 2003, May 2004, August 2004 and September 2004. In March 2004, the Company completed a securitization of its retained interest in eight securitization transactions previously sponsored by the Company and its affiliates, which was also structured as a secured financing. In addition, in June 2004, the Company completed a term securitization of Contracts purchased in the SeaWest Asset Acquisition and under the TFC Programs, which was structured as a secured financing. The Company's MFN and TFC subsidiaries completed term securitizations structured as secured financings prior to their becoming subsidiaries of the Company. The structures of the Company's two warehouse securitization transactions that related to the CPS Programs were amended in July 2003 to be treated as secured financings for financial accounting purposes. The Company's third warehouse securitization credit facility available to the Company at the time, which related to the TFC Programs, was structured as a secured financing for financial accounting purposes since the date of the TFC Merger. Such third warehouse facility expired on June 24, 2004.

The three-month period ended September 30, 2004 compared to the three-month period ended September 30, 2003

Revenues. During the three months ended September 30, 2004, revenues were \$32.3 million, an increase of \$6.2 million, or 23.9%, from the prior year period revenue amount of \$26.0 million. The primary reason for the increase in revenues is an increase in interest income. Interest income for the three-month period ended September 30, 2004 increased \$9.5 million, or 59.9%, to \$25.3 million in 2004 from \$15.8 million for the same period in 2003. The primary reasons for the increase in interest income are the change in securitization structure implemented during the third quarter of 2003 as described above and the interest income earned on the portfolios of Contracts acquired in the SeaWest Asset Acquisition. Those increases were partially offset by the decline in the balance of the portfolio of Contracts acquired in the MFN Merger and the TFC Merger, and an impairment loss of \$2.6 million related to the Company's analysis and estimate of the expected ultimate performance of the Company's previously securitized pools which are held by non-consolidated subsidiaries.

The interest income is additionally offset in part by a decrease in servicing fees. Servicing fees of \$3.0 million in the three months ended September 30, 2004 decreased \$1.3 million, or 29.4%, from \$4.3 million in the same period a year earlier. The decrease in servicing fees is the result of the change in securitization structure and the consequent decline in the Company's managed portfolio held by non-consolidated subsidiaries. The decrease was partially offset by the servicing fees earned on the SeaWest Third Party Portfolio. The Contracts in the Company's managed portfolio held by non-consolidated subsidiaries were securitized in structures treated as sales for financial accounting purposes and, therefore, do not appear on the Company's Unaudited Condensed Consolidated Balance Sheet. As a result of the decision to structure future securitizations as secured financings, the Company's managed portfolio held by non-consolidated subsidiaries will continue to decline in future periods, and servicing fee revenue is anticipated to continue to decline proportionately. As of September 30, 2004 and 2003, the Company's

managed portfolio owned by consolidated vs. non-consolidated subsidiaries and other third parties was as follows:

	September 30, 2004		September 30, 2003	
	Amount	%	Amount	%
Total Managed Portfolio	(Dollars in millions)			
Owned by Consolidated Subsidiaries.....	\$ 553.9	61.6%	\$ 275.1	36.6%
Owned by Non-Consolidated Subsidiaries.....	276.2	30.8%	477.2	63.4%
SeaWest Third Party Portfolio.....	68.2	7.6%	-	0.0%
Total.....	<u>\$ 898.3</u>	<u>100.0%</u>	<u>\$ 752.3</u>	<u>100.0%</u>

At September 30, 2004, the Company was generating income and fees on a managed portfolio with an outstanding principal balance approximating \$898.3 million (this amount includes \$68.2 million related to the SeaWest Third Party Portfolio on which the Company earns only servicing fees), compared to a managed portfolio with an outstanding principal balance approximating \$752.3 million as of September 30, 2003. As the portfolio of Contracts acquired in the MFN Merger and the TFC Merger decreases, the portfolio of Contracts originated under the CPS Programs continues to expand. At September 30, 2004 and 2003, the managed portfolio composition was as follows:

	September 30, 2004		September 30, 2003	
	Amount	%	Amount	%
Originating Entity	(Dollars in millions)			
CPS.....	\$ 660.5	73.6%	\$ 517.8	68.8%
TFC.....	93.2	10.3%	137.9	18.3%
MFN.....	26.7	3.0%	96.6	12.9%
SeaWest.....	49.7	5.5%	-	-
SeaWest Third Party Portfolio.....	68.2	7.6%	-	-
Total.....	<u>\$ 898.3</u>	<u>100.0%</u>	<u>\$ 752.3</u>	<u>100.0%</u>

Other income decreased \$2.0 million, or 33.7%, to \$3.9 million during the quarter ended September 30, 2004 from \$5.9 million during the same 2003 period. The period over period decrease resulted primarily from a sales tax refund of \$2.0 million received in the 2003 period.

Expenses. The Company's operating expenses consist primarily of personnel costs and other operating expenses, which are incurred as applications and Contracts are received, processed and serviced. Factors that affect margins and net earnings include changes in the automobile and automobile finance market environments and macroeconomic factors such as interest rates and the unemployment level.

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

Other operating expenses include interest expense, provision for credit losses, facilities expenses, telephone and other communication services, credit services, computer services (including personnel costs associated with information technology support), professional services, marketing and advertising expenses, and depreciation and amortization.

Total operating expenses were \$34.3 million for the third quarter of 2004, compared to \$28.9 million for the third quarter of 2003. The increase is primarily due to the \$3.4 million increase in the provision for credit losses to \$7.6 million during the 2004 period as compared to \$4.2 million in the 2003 period. Increased interest expense also contributed. These increases were partially offset by reduced general and administrative expenses.

Personnel costs increased slightly to \$9.9 million during the three months ended September 30, 2004, representing 28.9% of total operating expenses, from \$9.5 million for the comparable 2003 period, or 32.8% of total operating expenses. The decrease as a percentage of total operating expenses reflects the higher operating expenses incurred in the current period, primarily a result of the increased provision for credit losses and interest expense.

General and administrative expenses decreased to \$4.8 million, or 13.9% of total operating expenses, in the third quarter of 2004, as compared to \$6.1 million, or 20.9% of total operating expenses, in the third quarter of 2003. The decrease is due primarily to reduced corporate legal expenses as compared to the 2003 period.

Interest expense for the three-month period ended September 30, 2004, increased \$2.0 million, or 30.5%, to \$8.4 million, compared to \$6.4 million in the comparable period in 2003. The increase is primarily the result of changes in the amount and composition of securitization trust debt carried on the Company's Unaudited Condensed Consolidated Balance Sheet. Such debt increased as a result of the SeaWest Asset Acquisition and the change in securitization structure implemented beginning in July 2003, partially offset by the decrease in the balance of the securitization trust debt acquired in the MFN Merger and the TFC Merger. As the Company continues to structure future securitization transactions as secured financings, securitization trust debt and the related interest expense are expected to increase.

Marketing expense for the three-month period ended September 30, 2004, increased \$1.2 million, or 84.6%, to \$2.6 million, compared to \$1.4 million in the comparable period in 2003. The increase is primarily the result of subscription fees associated with dealer application software initially implemented in the first quarter of 2004.

The Company increased its valuation allowance against the net deferred tax asset by the income tax benefit for the 2004 period. The result is a net income tax provision of zero for the three-month period ended September 30, 2004. No income tax expense was recorded during the 2003 period.

The nine-month period ended September 30, 2004 compared to the nine-month period ended September 30, 2003

Revenues. During the nine months ended September 30, 2004, revenues were \$92.5 million, an increase of \$19.2 million, or 26.2%, from the prior year period revenue amount of \$73.3 million. The primary reason for the increase in revenues is an increase in interest income. Interest income for the nine-month period ended September 30, 2004 increased \$34.9 million, or 95.2%, to \$71.5 million in 2004 from \$36.6 million in 2003. The primary reasons for the increase in interest income are the change in securitization structure implemented during the third quarter of 2003 as described above and the interest income earned on the portfolios of Contracts acquired in the TFC Merger and the SeaWest Asset Acquisition. This increase was partially offset by the decline in the balance of the portfolio of Contracts acquired in the MFN Merger and a decrease in residual interest income, including an impairment loss of \$2.6 million related to the Company's analysis and estimate of the expected ultimate performance of the Company's previously securitized pools that are held by non-consolidated subsidiaries.

The increase in interest income is offset in part by the elimination of net gain on sale of Contracts revenue and a decrease in servicing fees. As a result of the change in securitization structure, zero net gain on sale of Contracts was recorded in the current period, compared to \$8.7 million net gain on sale in the year earlier period. The 2003 gain on sale of Contracts amount is net of a negative fair value adjustment of \$1.8 million related to the Company's analysis and estimate of the expected ultimate performance of the Company's previously securitized pools that are held by non-consolidated subsidiaries.

Servicing fees of \$9.9 million in the nine months ended September 30, 2004 decreased \$3.5 million, or 26.2%, from \$13.4 million in the same period a year earlier. The decrease in servicing fees is the result of the change in securitization structure and the consequent decline in the Company's managed portfolio

held by non-consolidated subsidiaries. The decrease was partially offset by the servicing fees earned on the SeaWest Third Party Portfolio.

Other income decreased \$3.5 million, or 24.0%, to \$11.2 million during the nine months ended September 30, 2004 from \$14.7 million during the 2003 period. The period over period decrease resulted primarily from a sales tax refund of \$2.0 received in the 2003 period and decreased recoveries on previously charged off MFN Contracts. Such recoveries were \$6.4 million for the nine months ended September 30, 2004, compared to \$9.6 million for the same period in 2003.

Expenses. The Company's operating expenses consist primarily of personnel costs and other operating expenses, which are incurred as applications and Contracts are received, processed and serviced. Factors that affect margins and net earnings include changes in the automobile and automobile finance market environments and macroeconomic factors such as interest rates and the unemployment level.

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

Other operating expenses include interest expense, provision for credit losses, facilities expenses, telephone and other communication services, credit services, computer services (including personnel costs associated with information technology support), professional services, marketing and advertising expenses, and depreciation and amortization.

Total operating expenses were \$96.1 million for the first nine months of 2004, compared to \$70.7 million for the first nine months of 2003. The increase is primarily due to a \$16.4 million increase in the provision for credit losses to \$20.6 million during the 2004 period as compared to \$4.2 million in the 2003 period. Increased interest expense and personnel costs were also significant.

Personnel costs increased to \$29.4 million during the nine months ended September 30, 2004, representing 30.5% of total operating expenses, from \$27.4 million for the comparable 2003 period, or 38.7% of total operating expenses. The increase is primarily the result of staff additions related to the TFC Merger in May 2003 and the SeaWest Asset Acquisition in April 2004. This increase was partially offset by staff reductions since the MFN Merger in 2002 related to the integration and consolidation of certain service and administrative activities and the decline in the balance of the portfolio of Contracts acquired in the MFN Merger. The decrease as a percentage of total operating expenses reflects the higher operating expenses, primarily a result of the increased provision for credit losses and interest expense.

General and administrative expenses increased to \$15.2 million, or 15.8% of total operating expenses, in the first nine months of 2004, as compared to \$14.1 million, or 20.0% of total operating expenses, in the first nine months of 2003. The increase is due primarily to increased legal expenses and incremental corporate expenses associated with the TFC Merger, which closed in May 2003. The decrease as a percentage of total operating expenses reflects the higher operating expenses primarily a result of the provision for credit losses and interest expense.

Interest expense for the nine-month period ended September 30, 2004, increased \$4.8 million, or 27.9%, to \$21.8 million, compared to \$17.0 million in the comparable period in 2003. The increase is primarily the result of changes in the amount and composition of securitization trust debt carried on the Company's Unaudited Condensed Consolidated Balance Sheet. Such debt increased as a result of the TFC Merger and the SeaWest Asset Acquisition and the change in securitization structure implemented beginning in July 2003, partially offset by the decrease in the balance of the securitization trust debt acquired in the MFN Merger.

Marketing expense for the nine-month period ended September 30, 2004, increased \$1.8 million, or 42.9%, to \$5.9 million, compared to \$4.1 million in the comparable period in 2003. The increase is

primarily the result of subscription fees associated with dealer application software initially implemented in the first quarter of 2004.

The Company increased its valuation allowance against the net deferred tax asset by the income tax benefit for the 2004 periods presented. The result is a net income tax provision of zero for the three- and nine-month periods ended September 30, 2004. In the 2003 period, an income tax benefit of \$3.4 million was recorded. The income tax benefit in the prior period was primarily the result of the resolution of certain IRS examinations of tax returns filed by MFN prior to the MFN Merger. The resulting tax benefit of \$4.9 million was offset in part by an income tax provision of \$1.5 million.

Liquidity and Capital Resources

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

Net cash provided by operating activities for the nine-month periods ended September 30, 2004 and 2003 was \$10.3 million and \$64.2 million, respectively. Cash from operating activities is generally provided by the net releases from the Company's securitization Trusts.

Net cash used in investing activities for the nine-month periods ended September 30, 2004 and 2003 was \$241.2 million and \$101.0 million, respectively. Cash used in investing activities has generally related to purchases of Contracts, the cost of acquiring TFC and the purchase of furniture and equipment.

Net cash provided by financing activities for the nine months ended September 30, 2004, was \$208.6 million compared with net cash used in financing activities of \$30.9 million for the nine months ended September 30, 2003. Cash used or provided by financing activities is primarily attributable to the repayment or issuance of debt.

The primary reason for the significant increase in cash used in investing activities and cash provided by financing activities period over period is the change in the securitization structure implemented in the third quarter of 2003.

Contracts are purchased from Dealers for a cash price generally approximating their principal amount, and generate cash flow over a period of years. As a result, the Company has been dependent on warehouse credit facilities to purchase Contracts, and on the availability of cash from outside sources in order to finance its continuing operations, as well as to fund the portion of Contract purchase prices not financed under warehouse credit facilities. As of September 30, 2004 the Company had \$225 million in warehouse credit capacity, in the form of a \$125 million facility and a \$100 million facility. Both warehouse facilities provide funding for Contracts purchased under the CPS Programs. A third facility in the amount of \$75 million, which the Company utilized to fund Contracts under the CPS Programs,

expired on February 21, 2004. A fourth facility in the amount of \$25 million, which the Company utilized to fund Contracts under the TFC Programs, expired on June 24, 2004.

The \$125 million warehouse facility is structured to allow the Company to fund a portion of the purchase price of Contracts by drawing against a floating rate variable funding note issued by CPS Warehouse Trust. This facility was established on March 7, 2002, in the maximum amount of \$100 million. Such maximum amount was increased to \$125 million in November 2002. Approximately 73% of the principal balance of Contracts may be advanced to the Company under this facility, subject to collateral tests and certain other conditions and covenants. Notes under this facility bear interest at a rate of one-month commercial paper plus 1.18% per annum. This facility was renewed in April 2004 and expires on April 3, 2005.

The \$100 million warehouse facility is similarly structured to allow CPS to fund a portion of the purchase price of Contracts by drawing against a floating rate variable funding note issued by Page Funding LLC. Approximately 73.5% of the principal balance of Contracts may be advanced to the Company under this facility, subject to collateral tests and certain other conditions and covenants. Notes under this facility accrue interest at a rate of one-month LIBOR plus 1.50% per annum. This facility was entered into on June 30, 2004 and expires on June 30, 2007. The lender has annual termination options.

The \$75 million warehouse facility was similarly structured to allow CPS to fund a portion of the purchase price of Contracts by drawing against a floating rate variable funding note issued by CPS Funding LLC. Approximately 72.5% of the principal balance of Contracts could be advanced to the Company under this facility, subject to collateral tests and certain other conditions and covenants. Notes under this facility accrued interest at a rate of one-month LIBOR plus 0.75% per annum. This facility expired on February 21, 2004.

The \$25 million warehouse facility was similarly structured to allow TFC to fund a portion of the purchase price of Contracts by drawing against a floating rate variable funding note issued by TFC Warehouse I LLC. Approximately 71% of the principal balance of Contracts could be advanced to TFC under this facility, subject to collateral tests and certain other conditions and covenants. Notes under this facility accrued interest at a rate of one-month LIBOR plus 1.75% per annum. This facility was entered into as part of the TFC Merger on May 20, 2003 and expired on June 24, 2004. The Company is currently in discussions with several parties regarding a replacement facility.

These facilities are independent of each other. With the two currently existing facilities, two different financial institutions purchase the notes issued by these facilities, and two different insurers insure the notes (each a "Note Insurer"). The Note Insurer on the \$125 million facility is the controlling party whereas the lender on the \$100 million facility is the controlling party. Up through June 30, 2003, sales of Contracts to the special purpose subsidiaries ("SPS") related to two of the three then existing facilities had been treated as sales for financial accounting purposes. The Company, therefore, removed these securitized Contracts and related debt from its Unaudited Condensed Consolidated Balance Sheet and recognized a gain on sale in the Company's Unaudited Condensed Consolidated Statement of Operations related to Contracts financed through this facility. Indebtedness related to Contracts funded by the third facility existing as of June 30, 2003, however, was on the Company's Unaudited Condensed Consolidated Balance Sheet and no gain on sale has ever been recognized in the Company's Unaudited Condensed Consolidated Statement of Operations. During July 2003, each of the first two facilities was amended, with the effect that subsequent use of such facilities is treated for financial accounting purposes as a borrowing secured by such receivables, rather than as a sale of receivables. The effects of that amendment are similar to those discussed above with respect to the change in securitization structure. Both existing facilities as of September 30, 2004 are treated for financial accounting purposes as secured financings.

For the portfolio owned by non-consolidated subsidiaries, cash used to increase Credit Enhancement amounts to required levels for the nine-month periods ended September 30, 2004 and 2003 was \$2.1 million and \$19.6 million, respectively. Cash released from Trusts and their related Spread Accounts to

the Company for the nine-month periods ended September 30, 2004 and 2003, was \$17.2 million and \$20.2 million, respectively. Changes in the amount of Credit Enhancement required for term securitization transactions and releases from Trusts and their related Spread Accounts are affected by the relative size, seasoning and performance of the various pools of Contracts securitized that make up the Company's managed portfolio to which the respective Spread Accounts are related. The Company did not make any initial deposits to Spread Accounts or fund initial overcollateralization related to term securitization transactions owned by non-consolidated subsidiaries during the nine months ended September 30, 2004 compared to \$18.7 million during the nine months ended September 30, 2003.

The acquisition of Contracts for subsequent sale in securitization transactions, and the need to fund Spread Accounts and initial overcollateralization, if any, and increase Credit Enhancement levels when those transactions take place, results in a continuing need for capital. The amount of capital required is most heavily dependent on the rate of the Company's Contract purchases, the advance rate on the warehouse facilities, the required level of initial Credit Enhancement in securitizations, and the extent to which the previously established Trusts and their related Spread Accounts either release cash to the Company or capture cash from collections on securitized Contracts. The Company is limited in its ability to purchase Contracts by its available cash and the capacity of its warehouse facilities. As of September 30, 2004, the Company had unrestricted cash on hand of \$10.9 million and available Contract purchase commitments financing from its warehouse credit facilities of \$208.5 million, subject to collateral availability. The Company's plans to manage its need for liquidity include the completion of additional term securitizations that would provide additional credit availability from the warehouse credit facilities, and matching its levels of Contract purchases to its availability of cash. There can be no assurance that the Company will be able to complete term securitizations on favorable economic terms or that the Company will be able to complete term securitizations at all. If the Company is unable to complete such securitizations, interest income and other portfolio related income would decrease.

The Company's primary means of ensuring that its cash demands do not exceed its cash resources is to match its levels of Contract purchases to its availability of cash. The Company's ability to adjust the quantity of Contracts that it purchases and securitizes will be subject to general competitive conditions and the continued availability of warehouse credit facilities. There can be no assurance that the desired level of Contract acquisition can be maintained or increased. Obtaining releases of cash from the Trusts and their related Spread Accounts is dependent on collections from the related Trusts generating sufficient cash to maintain the Spread Accounts in excess of their respective requisite levels. There can be no assurance that collections from the related Trusts will continue to generate sufficient cash.

Certain of the Company's securitization transactions and the warehouse credit facilities contain various covenants requiring certain minimum financial ratios and results. As a result of amendments to the related Securitization Agreements executed during the first nine months of 2004, the Company was in compliance with all of these covenants as of September 30, 2004, except one related to the minimum cash balance on the closing date of a term securitization transaction. The controlling party has waived this covenant breach.

The Securitization Agreements of the Company's term securitization transactions and one of the warehouse credit facilities are terminable by the Note Insurers in the event of certain defaults by the Company and under certain other circumstances. Similar termination rights are held by the lender in the other warehouse credit facility. Were a Note Insurer (or the lender in such warehouse facility) in the future to exercise its option to terminate the Securitization Agreements, such a termination would have a material adverse effect on the Company's liquidity and results of operations. The Company continues to receive Servicer extensions on a monthly and/or quarterly basis, pursuant to the Securitization Agreements.

Critical Accounting Policies

(a) Allowance for Finance Credit Losses

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

(b) Treatment of Securitizations

Gain on sale may be recognized on the disposition of Contracts either outright or in securitization transactions. In those securitization transactions that were treated as sales for financial accounting purposes, the Company, or a wholly-owned, consolidated subsidiary of the Company, retains a residual interest in the Contracts that were sold to a wholly-owned, unconsolidated special purpose subsidiary. The Company's securitization transactions include "term" securitizations (the purchaser holds the Contracts for substantially their entire term) and "continuous" or "warehouse" securitizations (which finance the acquisition of the Contracts for future sale into term securitizations).

As of September 30, 2004 and December 31, 2003 the line item "Residual interest in securitizations" on the Company's Unaudited Consolidated Balance Sheet represents the residual interests in certain term securitizations but no residual interest in warehouse securitizations, because the Company's warehouse securitizations were restructured in July 2003 as secured financings. Subsequent term securitizations of receivables purchased were also structured as secured financings. The warehouse securitizations are accordingly reflected in the line items "Finance receivables" and "Warehouse lines of credit" on the Company's Unaudited Condensed Consolidated Balance Sheet, and the term securitizations are reflected in the line items "Finance receivables" and "Securitization trust debt." The "Residual interest in securitizations" represents the discounted sum of expected future releases from securitization trusts. Accordingly, the valuation of the residual is heavily dependent on estimates of future performance.

The Company's securitization structure is generally as follows:

The Company sells Contracts it acquires to a wholly-owned Special Purpose Subsidiary ("SPS"), which has been established for the limited purpose of buying and reselling the Company's Contracts. The SPS then transfers the same Contracts to another entity, typically a statutory trust ("Trust"). The Trust issues interest-bearing asset backed securities (the "Notes"), generally in a principal amount equal to the aggregate principal balance of the Contracts. The Company typically sells these Contracts to the Trust at face value and without recourse, except that representations and warranties similar to those provided by the Dealer to the Company are provided by the Company to the Trust. One or more investors purchase the Notes issued by the Trust; the proceeds from the sale of the Notes are then used to purchase the Contracts from the Company. The Company may retain or sell subordinated Notes issued by the Trust. The Company purchases a financial guaranty insurance policy, guaranteeing timely payment of principal and interest on the senior Notes, from a Note Insurer. In addition, the Company provides "Credit Enhancement" for the benefit of the Note Insurer and the investors in the form of an initial cash deposit to a bank account (a "Spread Account") held by the Trust, in the form of overcollateralization of the Notes, where the principal balance of the Notes issued is less than the principal balance of the Contracts, in the form of subordinated Notes, or some combination of such Credit Enhancements. The agreements governing the securitization transactions (collectively referred to as the "Securitization Agreements") require that the initial level of Credit Enhancement be supplemented by a portion of collections from the

Contracts until the level of Credit Enhancement reaches specified levels, and then maintained at those levels. The specified levels are generally computed as a percentage of the principal amount remaining unpaid under the related Contracts. The specified levels at which the Credit Enhancements are to be maintained will vary depending on the performance of the portfolios of Contracts held by the Trusts and on other conditions, and may also be varied by agreement among the Company, the SPS, the Note Insurers and the trustee. Such levels have increased and decreased from time to time based on performance of the portfolios, and have also varied by Securitization Agreement. The Securitization Agreements generally grant the Company the option to repurchase the sold Contracts from the Trust when the aggregate outstanding balance has amortized to a specified percentage of the initial aggregate balance.

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

The Company’s warehouse securitization structures are similar to the above, except that (i) the SPS that purchases the Contracts pledges the Contracts to secure promissory notes which it issues, (ii) the promissory notes are in an aggregate principal amount of not more than 73.0% to 73.5% of the aggregate principal balance of the Contracts (that is, at least 26.5% overcollateralization), and (iii) no increase in the required amount of Credit Enhancement is contemplated unless certain portfolio performance tests are breached. During the quarter ended September 30, 2003 the warehouse securitizations related to the CPS Programs were amended to provide for the transactions to be reflected as secured financings for financial accounting purposes. The Contracts held by the warehouse SPS and the promissory notes that it issues are therefore included in the Company’s Unaudited Condensed Consolidated Financial Statements as of September 30, 2004 and December 31, 2003 as assets and liabilities, respectively.

Upon each sale of Contracts in a securitization structured as a secured financing, whether a term securitization or a warehouse securitization, the Company retains on its Unaudited Condensed Consolidated Balance Sheet the Contracts securitized as assets and records the Notes issued in the transaction as indebtedness of the Company.

Under the prior securitizations structured as sales for financial accounting purposes, the Company removed from its Unaudited Condensed Consolidated Balance Sheet the Contracts sold and added to its Unaudited Condensed Consolidated Balance Sheet (i) the cash received, if any, and (ii) the estimated fair value of the ownership interest that the Company retains in Contracts sold in the securitization. That retained or residual interest (the “Residual”) consists of (a) the cash held in the Spread Account, if any, (b) overcollateralization, if any, (c) subordinated Notes retained, if any, and (d) receivables from Trust, which include the net interest receivables (“NIRs”). NIRs represent the estimated discounted cash flows to be received from the Trust in the future, net of principal and interest payable with respect to the Notes, and certain expenses. The excess of the cash received and the assets retained by the Company over the carrying value of the Contracts sold, less transaction costs, equals the net gain on sale of Contracts recorded by the Company. Until the maturity of these transactions, the Company’s Unaudited Condensed Consolidated Balance Sheet will reflect securitization transactions structured both as sales and as secured financings.

With respect to the prior securitizations structured as sales for financial accounting purposes, the Company allocates its basis in the Contracts between the Notes sold and the Residuals retained based on the relative fair values of those portions on the date of the sale. The Company recognized gains or losses attributable to the change in the fair value of the Residuals, which are recorded at estimated fair value. The Company is not aware of an active market for the purchase or sale of interests such as the Residuals; accordingly, the Company determines the estimated fair value of the Residuals by discounting the amount and timing of anticipated cash flows that it estimates will be released to the Company in the future (the cash out method), using a discount rate that the Company believes is appropriate for the risks involved.

The anticipated cash flows include collections from both current and charged off receivables. The Company has used an effective pre-tax discount rate of approximately 14% per annum except for certain collections from charged off receivables related to the Company's securitizations in 2001 and later where the Company has used a discount rate of approximately 25%.

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

If the amount of cash required for payment of fees, interest and principal exceeds the amount collected during the collection period, the shortfall is withdrawn from the Spread Account, if any. If the cash collected during the period exceeds the amount necessary for the above allocations, and there is no shortfall in the related Spread Account or other form of Credit Enhancement, the excess is released to the Company, or in certain cases is transferred to other Spread Accounts that may be below their required levels. If the total Credit Enhancement amount is not at the required level, then the excess cash collected is retained in the Trust until the specified level is achieved. Although Spread Account balances are held by the Trusts on behalf of the Company's SPS as the owner of the Residuals (in the case of securitization transactions structured as sales for financial accounting purposes) or the Trusts (in the case of securitization transactions structured as secured financings for financial accounting purposes), the cash in the Spread Accounts is restricted from use by the Company. Cash held in the various Spread Accounts is invested in high quality, liquid investment securities, as specified in the Securitization Agreements. The interest rate payable on the Contracts is significantly greater than the interest rate on the Notes. As a result, the Residuals described above are a significant asset of the Company. In determining the value of the Residuals, the Company must estimate the future rates of prepayments, delinquencies, defaults and default loss severity, and recovery rates, as all of these factors affect the amount and timing of the estimated cash flows. The Company estimates prepayments by evaluating historical prepayment performance of comparable Contracts. As of September 30, 2004, the Company has used prepayment estimates of approximately 19.4% to 24.6% cumulatively over the lives of the related Contracts. The Company estimates defaults and default loss severity using available historical loss data for comparable Contracts and the specific characteristics of the Contracts purchased by the Company. The Company estimates recovery rates of previously charged off receivables using available historical recovery data and projected future recovery levels. In valuing the Residuals, the Company estimates that charge-offs as a percentage of the original principal balance will approximate 15.1% to 24.0% cumulatively over the lives of the related Contracts, with recovery rates approximating 2.6% to 5.6% of the original principal balance.

Following a securitization that is structured as a sale for financial accounting purposes, interest income is generally recognized on the balance of the Residuals at the same rate as used for calculating the present value of the NIRs, which is equal to 14% per annum. In addition, the Company will recognize additional revenue from the Residuals if the actual performance of the Contracts is better than the original estimate. If the actual performance of the Contracts were worse than the original estimate, then a downward adjustment to the carrying value of the Residuals and a related expense would be required. In a securitization structured as a secured financing for financial accounting purposes, interest income is recognized when accrued under the terms of the related Contracts and, therefore, presents less potential for fluctuations in performance when compared to the approach used in a transaction structured as a sale for financial accounting purposes.

In all the Company's term securitizations, whether treated as secured financings or as sales, the Company has sold the receivables (through a subsidiary) to the securitization Trust. The difference between the two structures is that in securitizations that are treated as secured financings the Company reports the assets and liabilities of the securitization Trust on its Consolidated Balance Sheet. Under both structures the Noteholders and the related securitization Trusts have no recourse to the Company for failure of the Contract obligors to make payments on a timely basis. The Company's Residuals, however, are subordinate to the Notes until the Noteholders are fully paid, and the Company is therefore at risk to that extent.

(c) Income taxes

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

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

Forward Looking Statements

This report on Form 10-Q includes certain "forward-looking statements," including, without limitation, the statements or implications to the effect that prepayments as a percentage of original balances will approximate 19.4% to 24.6% cumulatively over the lives of the related Contracts, that charge-offs as a percentage of original balances will approximate 15.1% to 24.0% cumulatively over the lives of the related Contracts, with recovery rates approximating 2.6% to 5.6% of original principal balances. Other forward-looking statements may be identified by the use of words such as "anticipates," "expects," "plans," "estimates," or words of like meaning. As to the specifically identified forward-looking statements, factors that could affect charge-offs and recovery rates include changes in the general economic climate, which could affect the willingness or ability of obligors to pay pursuant to the terms of Contracts, changes in laws respecting consumer finance, which could affect the ability of the Company to enforce rights under Contracts, and changes in the market for used vehicles, which could affect the levels of recoveries upon sale of repossessed vehicles. Factors that could affect the Company's revenues in the current year include the levels of cash releases from existing pools of Contracts, which would affect the Company's ability to purchase Contracts, the terms on which the Company is able to finance such purchases, the willingness of Dealers to sell Contracts to the Company on the terms that it offers, and the terms on which the Company is able to complete term securitizations once Contracts are acquired. Factors that could affect the Company's expenses in the current year include competitive conditions in the market for qualified personnel, and interest rates (which affect the rates that the Company pays on Notes issued in its securitizations). The statements concerning the Company structuring future securitization transactions as secured financings and the effects of such structures on financial items and on the Company's future profitability also are forward-looking statements. Any change to the structure of the Company's securitization transaction could cause such forward-looking statements not to be accurate. Both the amount of the effect of the change in structure on the Company's profitability and the duration

of the period in which the Company's profitability would be affected by the change in securitization structure are estimates. The accuracy of such estimates will be affected by the rate at which the Company purchases and sells Contracts, any changes in that rate, the credit performance of such Contracts, the financial terms of future securitizations, any changes in such terms over time, and other factors that generally affect the Company's profitability.

Additional risk factors, any of which could have a material effect on the Company's performance, are set forth below:

Dependence on Warehouse Financing. The Company's primary source of day-to-day liquidity is continuous securitization of Contracts, under which it sells or pledges Contracts, as often as once a week, to either of two special-purpose affiliated entities. Such transactions function as a "warehouse" in which Contracts are held. The Company expects to continue to effect similar transactions (or to obtain replacement or additional financing) as current arrangements expire or become fully utilized; however, there can be no assurance that such financing will be obtainable on favorable terms. To the extent that the Company is unable to maintain its existing structure or is unable to arrange new warehouse facilities, the Company may have to curtail Contract purchasing activities, which could have a material adverse effect on the Company's financial condition, results of operations and liquidity.

Dependence on Securitization Program. The Company is dependent upon its ability to continue to finance pools of Contracts in term securitizations in order to generate cash proceeds for new purchases. Adverse changes in the market for securitized Contract pools, or a substantial lengthening of the warehousing period, would burden the Company's financing capabilities, could require the Company to curtail its purchase of Contracts, and could have a material adverse effect on the Company. In addition, as a means of reducing the percentage of cash collateral that the Company would otherwise be required to deposit and maintain in Spread Accounts, all of the Company's securitizations since June 1994 have utilized credit enhancement in the form of financial guaranty insurance policies issued by monoline financial guaranty insurers. The Company believes that financial guaranty insurance policies reduce the costs of securitizations relative to alternative forms of credit enhancements available to the Company. No insurer is required to insure Company-sponsored securitizations and there can be no assurance that any will continue to do so. Similarly, there can be no assurance that any securitization transaction will be available on terms acceptable to the Company, or at all. The timing of any securitization transaction is affected by a number of factors beyond the Company's control, any of which could cause substantial delays, including, without limitation, market conditions and the approval by all parties of the terms of the securitization.

Risk of General Economic Downturn. The Company's business is directly related to sales of new and used automobiles, which are affected by employment rates, prevailing interest rates and other domestic economic conditions. Delinquencies, repossessions and losses generally increase during economic slowdowns or recessions. Because of the Company's focus on Sub-Prime Customers, the actual rates of delinquencies, repossessions and losses on such Contracts could be higher under adverse economic conditions than those experienced in the automobile finance industry in general. Any sustained period of economic slowdown or recession could adversely affect the Company's ability to sell or securitize pools of Contracts. The timing of any economic changes is uncertain, and sluggish sales of automobiles and weakness in the economy could have an adverse effect on the Company's business and that of the Dealers from which it purchases Contracts.

Dependence on Performance of Securitized Contracts. Under the financial structures the Company has used to date in its term securitizations, certain excess cash flows generated by the Contracts sold in the term securitizations are used to increase overcollateralization or are retained in a Spread Account within the securitization trusts to provide liquidity and credit enhancement. While the specific terms and mechanics of each Spread Account vary among transactions, the Company's Securitization Agreements generally provide that the Company will receive excess cash flows only if the amount of Credit Enhancement has reached specified levels and/or the delinquency or losses related to the Contracts in the pool are below certain

predetermined levels. In the event delinquencies and losses on the Contracts exceed such levels, the terms of the securitization: (i) may require increased Credit Enhancement to be accumulated for the particular pool; (ii) may restrict the distribution to the Company of excess cash flows associated with other pools; or (iii) in certain circumstances, may permit the insurers to require the transfer of servicing on some or all of the Contracts to another servicer. Any of these conditions could materially adversely affect the Company's liquidity, financial condition and operations.

Creditworthiness of Consumers. The Company specializes in the purchase, sale and servicing of Contracts to finance automobile purchases by Sub-Prime Customers, which entail a higher risk of non-performance, higher delinquencies and higher losses than Contracts with more creditworthy customers. While the Company believes that the underwriting criteria and collection methods it employs enable it to control the higher risks inherent in Contracts with Sub-Prime Customers, no assurance can be given that such criteria and methods will afford adequate protection against such risks. The Company has experienced fluctuations in the delinquency and charge-off performance of its Contracts. In the event that portfolios of Contracts sold and serviced by the Company experience greater defaults, higher delinquencies or higher net losses than anticipated, the Company's income could be negatively affected. A larger number of defaults than anticipated could also result in adverse changes in the structure of the Company's future securitization transactions, such as a requirement of increased cash collateral or other Credit Enhancement in such transactions.

Probable Increase in Cost of Funds. The Company's profitability is determined by, among other things, the difference between the rate of interest charged on the Contracts purchased by the Company and the rate of interest payable to purchasers of Notes issued in securitizations. The Contracts purchased by the Company generally bear finance charges close to or at the maximum permitted by applicable state law. The interest rates payable on such Notes are fixed, based on interest rates prevailing in the market at the time of sale. Consequently, increases in market interest rates tend to reduce the "spread" or margin between Contract finance charges and the interest rates required by investors and, thus, the potential operating profits to the Company from the purchase, securitization and servicing of Contracts. Operating profits expected to be earned by the Company on portfolios of Contracts previously securitized are insulated from the adverse effects of increasing interest rates because the interest rates on the related Notes were fixed at the time the Contracts were sold. With interest rates near historical lows as of the date of this report, it is reasonable to expect that interest rates will increase in the near to intermediate term. Any future increases in interest rates would likely increase the interest rates on Notes issued in future term securitizations and could have a material adverse effect on the Company's results of operations and liquidity.

Prepayments and Credit Losses. Gains from the sale of Contracts in the Company's past securitization transactions structured as sales for financial accounting purposes have constituted a significant portion of the revenue of the Company. A portion of the gains is based in part on management's estimates of future prepayments and credit losses and other considerations in light of then-current conditions. If actual prepayments with respect to Contracts occur more quickly than was projected at the time such Contracts were sold, as can occur when interest rates decline, or if credit losses are greater than projected at the time such Contracts were sold, a charge to income may be required and would be recorded in the period of adjustment. If actual prepayments occur more slowly or if net losses are lower than estimated with respect to Contracts sold, total revenue would exceed previously estimated amounts.

Provisions for credit losses are recorded in connection with the origination and throughout the life of Contracts that are held on the Company's Unaudited Condensed Consolidated Balance Sheet. Such provisions are based on management's estimates of charge-offs in light of then-current conditions. If actual credit losses in a given period exceed the allowance for credit losses, a provision for credit losses during the period would be required.

Competition. The automobile financing business is highly competitive. The Company competes with a number of national, local and regional finance companies. In addition, competitors or potential competitors include other types of financial services companies, such as commercial banks, savings and

loan associations, leasing companies, credit unions providing retail loan financing and lease financing for new and used vehicles and captive finance companies affiliated with major automobile manufacturers such as General Motors Acceptance Corporation and Ford Motor Credit Corporation. Many of the Company's competitors and potential competitors possess substantially greater financial, marketing, technical, personnel and other resources than the Company. Moreover, the Company's future profitability will be directly related to the availability and cost of its capital relative to that of its competitors. The Company's competitors and potential competitors include far larger, more established companies that have access to capital markets for unsecured commercial paper and investment grade rated debt instruments, and to other funding sources which may be unavailable to the Company. Many of these companies also have long-standing relationships with Dealers and may provide other financing to Dealers, including floor plan financing for the Dealers' purchases of automobiles from manufacturers, which is not offered by the Company. There can be no assurance that the Company will be able to continue to compete successfully.

Litigation. Because of the consumer-oriented nature of the industry in which the Company operates and the application of certain laws and regulations, industry participants are regularly named as defendants in class-action litigation involving alleged violations of federal and state laws and regulations and consumer law torts, including fraud. Many of these actions involve alleged violations of consumer protection laws. Although the Company is not involved in any such material consumer protection litigation, a significant judgment against the Company or within the industry in connection with any such litigation, or an adverse outcome in the litigation identified under the caption "Legal Proceedings" in this report and in the Company's most recently filed report on Form 10-K, could have a material adverse effect on the Company's financial condition, results of operations and liquidity.

Dependence on Dealers. The Company is dependent upon establishing and maintaining relationships with unaffiliated Dealers to supply it with Contracts. During the three- and nine-month periods ended September 30, 2004, no Dealer accounted for as much as 1.0% of the Contracts purchased by the Company. The Dealer Agreements do not require Dealers to submit a minimum number of Contracts for purchase by the Company. The failure of Dealers to submit Contracts that meet the Company's underwriting criteria would have a material adverse effect on the Company's financial condition, results of operations and liquidity.

Government Regulations. The Company's business is subject to numerous federal and state consumer protection laws and regulations, which, among other things: (i) require the Company to obtain and maintain certain licenses and qualifications; (ii) limit the interest rates, fees and other charges the Company is allowed to charge; (iii) limit or prescribe certain other terms of its Contracts; (iv) require the Company to provide specified disclosures; and (v) regulate certain servicing and collection practices and define its rights to repossess and sell collateral. An adverse change in existing laws or regulations, or in the interpretation thereof, the promulgation of any additional laws or regulations, or the failure to comply with such laws and regulations could have a material adverse effect on the Company's financial condition, results of operations and liquidity.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risk

The Company is subject to interest rate risk during the period between when Contracts are purchased from Dealers and when such Contracts become part of a term securitization. Specifically, the interest rates on the warehouse facilities are adjustable while the interest rates on the Contracts are fixed. Historically, the Company's term securitization facilities have had fixed rates of interest. To mitigate some of this risk, the Company has in the past, and intends to continue to, structure certain of its securitization transactions to include pre-funding structures, whereby the amount of Notes issued exceeds the amount of Contracts initially sold to the Trusts. In pre-funding, the proceeds from the pre-funded portion are held in an escrow

account until the Company sells the additional Contracts to the Trust in amounts up to the balance of the pre-funded escrow account. In pre-funded securitizations, the Company locks in the borrowing costs with respect to the Contracts it subsequently delivers to the Trust. However, the Company incurs an expense in pre-funded securitizations equal to the difference between the money market yields earned on the proceeds held in escrow prior to subsequent delivery of Contracts and the interest rate paid on the Notes outstanding, the amount as to which there can be no assurance.

The Company is subject to market risks due to fluctuations in interest rates primarily as a result of its commitments to enter into new Contracts. The table below outlines the carrying values and estimated fair values of financial instruments:

	September 30, 2004		December 31, 2003	
	Carrying Value	Fair Value	Carrying Value	Fair Value
	(In thousands)			
Financial Instrument				
Finance receivables, net.....	\$ 485,922	485,922	\$ 266,189	266,189
Residual interest in securitizations.....	68,714	68,714	111,702	111,702
Warehouse lines of credit.....	16,521	16,521	33,709	33,709
Notes payable.....	1,593	1,593	3,330	3,330
Residual interest financing.....	27,311	27,311	-	-
Securitization trust debt.....	477,891	477,891	245,118	245,118
Senior secured debt.....	59,829	59,829	49,965	49,965
Subordinated debt.....	15,000	15,750	35,000	35,506
Related party debt.....	-	-	17,500	17,763

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

ITEM 4. CONTROLS AND PROCEDURES

CPS maintains a system of internal controls and procedures designed to provide reasonable assurance as to the reliability of its published financial statements and other disclosures included in this report. As of the end of the period covered by this report, CPS evaluated the effectiveness of the design and operation of such disclosure controls and procedures. Based upon that evaluation, the principal executive officer (Charles E. Bradley, Jr.) and the principal financial officer (Robert E. Riedl) concluded that the disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, material information relating to CPS that is required to be included in its reports filed under the Securities Exchange Act of 1934. There have been no significant changes in our internal controls over financial reporting during our most recently completed fiscal quarter that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II — OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The information provided under the caption “Legal Proceedings” in the Company’s Annual Report on Form 10-K for the year ended December 31, 2003, is incorporated herein by reference. In addition, the reader should be aware of the following:

On June 2, 2004, Delmar Coleman filed a lawsuit in the circuit court of Tuscaloosa, Alabama, making allegations similar to those that were asserted in the *Lang* case, and seeking damages in an unspecified amount, on behalf of a purported nationwide class. (The *Lang* case has been settled on the terms disclosed in the Annual Report, and related to alleged defects in the notices given with respect to repossessed vehicles.) CPS believes that it has one or more defenses to each of the claims made in this lawsuit, and intends to defend the matter vigorously.

On June 15, 2004, Keywana Booker filed a lawsuit in the federal district court of Atlanta, Georgia, alleging violations of the Fair Debt Collection Practices Act, and seeking damages in an unspecified amount on behalf of a purported class of Georgia residents. The Company has reached an agreement in principle to settle the *Booker* lawsuit payment of an immaterial amount.

On July 14, 2004, Jeremy Henry filed a lawsuit in the superior court of San Diego, California, alleging that he, and a purported California class, were harmed by alleged defects in post-repossession notices. The notice in question is a form that was used by TFC prior to TFC’s having been acquired by CPS, and for a short time thereafter. CPS believes that it has one or more defenses to each of the claims made in the lawsuit, and intends to defend this matter vigorously.

The Company is routinely involved in various legal proceedings resulting from its consumer finance activities and practices, both continuing and discontinued. The Company believes that there are substantive legal defenses to such claims, and intends to defend them vigorously. There can be no assurance, however, as to the outcome.

ITEM 2. CHANGES IN SECURITIES, USE OF PROCEEDS AND ISSUER PURCHASES OF EQUITY SECURITIES

During the three months ended September 30, 2004, the Company did not purchase any shares of its common stock.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) The following exhibits are filed with this report:

- 31.1 Rule 13a-14(a) Certification of the Chief Executive Officer of the registrant.
- 31.2 Rule 13a-14(a) Certification of the Chief Financial Officer of the registrant.
- 32 Section 1350 Certifications.*

* These Certifications shall not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liability of that section. These Certifications shall not be deemed to be incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Exchange Act, except to the extent that the registration statement specifically states that such Certifications are incorporated therein.

(b) The Company filed one report on Form 8-K during the quarter for which this report is filed. Such report was filed on August 3, 2004. It reported information under item 12 of Form 8-K, to the effect that the Company had issued a quarterly earnings release. Pursuant to Item 7, the text of such release was attached as an exhibit.

SIGNATURES

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

CONSUMER PORTFOLIO SERVICES, INC.

(Registrant)

Date: November 15, 2004

/s/ CHARLES E. BRADLEY, JR.

Charles E. Bradley, Jr.

President and Chief Executive Officer

(Principal Executive Officer)

Date: November 15, 2004

/s/ ROBERT E. RIEDL

Robert E. Riedl

Senior Vice President and Chief Financial Officer

(Principal Financial Officer)

CERTIFICATION

I, Charles E. Bradley, Jr., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Consumer Portfolio Services, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 15, 2004

/s/ CHARLES E. BRADLEY, JR.

Chief Executive Officer

CERTIFICATION

I, Robert E. Riedl, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Consumer Portfolio Services, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 15, 2004

/s/ ROBERT E. RIEDL

Chief Financial Officer

**Certification Pursuant To
18 U.S.C. Section 1350,
As Adopted Pursuant To
Section 906 of The Sarbanes-Oxley Act Of 2002**

In connection with the Quarterly Report on Form 10-Q of Consumer Portfolio Services, Inc. (the “Company”) for the quarterly period ended September 30, 2004, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), Charles E. Bradley, Jr., as Chief Executive Officer of the Company, and Robert E. Riedl, as Chief Financial Officer of the Company, each hereby certifies, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ CHARLES E. BRADLEY, JR.

Charles E. Bradley, Jr.
Chief Executive Officer
November 15, 2004

/s/ ROBERT E. RIEDL

Robert E. Riedl
Chief Financial Officer
November 15, 2004

This certification accompanies each Report pursuant to § 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of §18 of the Securities Exchange Act of 1934, as amended.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.