

PRA GROUP INC

Form 10-Q

May 10, 2016

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

---

FORM 10-Q

ý Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended March 31, 2016

¨ 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: 000-50058

---

PRA Group, Inc.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

75-3078675

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

120 Corporate Boulevard, Norfolk, Virginia

23502

(888) 772-7326

(Address of principal executive offices)

(Zip Code)

(Registrant's Telephone No., including area code)

Not

Applicable

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES ☒ NO ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one): Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☒ Smaller reporting company ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES ☐ NO ☒

The number of shares of the registrant's common stock outstanding as of May 6, 2016 was 46,328,722.

---

Table of Contents

Part I. Financial Information

Item 1.	<u>Financial Statements</u>	<u>3</u>
	<u>Consolidated Balance Sheets</u>	<u>3</u>
	<u>Consolidated Income Statements</u>	<u>4</u>
	<u>Consolidated Statements of Comprehensive Income/(Loss)</u>	<u>5</u>
	<u>Consolidated Statement of Changes in Equity</u>	<u>6</u>
	<u>Consolidated Statements of Cash Flows</u>	<u>7</u>
	<u>Notes to Consolidated Financial Statements</u>	<u>8</u>
	<u>1. Organization and Business</u>	<u>8</u>
	<u>2. Finance Receivables, net</u>	<u>9</u>
	<u>3. Investments</u>	<u>10</u>
	<u>4. Borrowings</u>	<u>11</u>
	<u>5. Property and Equipment, net</u>	<u>14</u>
	<u>6. Goodwill and Intangible Assets, net</u>	<u>15</u>
	<u>7. Share-Based Compensation</u>	<u>15</u>
	<u>8. Income Taxes</u>	<u>16</u>
	<u>9. Earnings per Share</u>	<u>17</u>
	<u>10. Commitments and Contingencies</u>	<u>18</u>
	<u>11. Fair Value</u>	<u>19</u>
	<u>12. Recent Accounting Pronouncements</u>	<u>21</u>
	<u>13. Subsequent Event</u>	<u>23</u>
Item 2.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>24</u>
Item 3.	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>47</u>
Item 4.	<u>Controls and Procedures</u>	<u>47</u>

Part II. Other Information

Item 1.	<u>Legal Proceedings</u>	<u>49</u>
Item 1A.	<u>Risk Factors</u>	<u>49</u>
Item 2.	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>49</u>
Item 3.	<u>Defaults Upon Senior Securities</u>	<u>49</u>
Item 4.	<u>Mine Safety Disclosures</u>	<u>49</u>
Item 5.	<u>Other Information</u>	<u>49</u>
Item 6.	<u>Exhibits</u>	<u>49</u>
	Signatures	<u>50</u>

Part I. Financial Information  
Item 1. Financial Statements

PRA Group, Inc.  
Consolidated Balance Sheets  
March 31, 2016 and December 31, 2015  
(unaudited)  
(Amounts in thousands)

	March 31, 2016	December 31, 2015
Assets		
Cash and cash equivalents	\$79,442	\$71,372
Investments	71,413	73,799
Finance receivables, net	2,377,077	2,202,113
Other receivables, net	33,555	30,771
Income taxes receivable	—	1,717
Net deferred tax asset	15,571	13,068
Property and equipment, net	47,785	45,394
Goodwill	524,870	495,156
Intangible assets, net	32,154	23,788
Other assets	86,966	33,389
Total assets	\$3,268,833	\$2,990,567
Liabilities and Equity		
Liabilities:		
Accounts payable	\$2,377	\$4,190
Accrued expenses	95,049	95,380
Income taxes payable	28,114	21,236
Net deferred tax liability	269,201	261,498
Interest-bearing deposits	55,349	46,991
Borrowings	1,896,424	1,717,129
Other liabilities	13,577	4,396
Total liabilities	2,360,091	2,150,820
Equity:		
Preferred stock, par value \$0.01, authorized shares, 2,000, issued and outstanding shares, 0—	—	—
Common stock, par value \$0.01, authorized shares, 100,000, issued and outstanding shares, 46,328 at March 31, 2016; 100,000 authorized shares, 46,173 issued and outstanding shares at December 31, 2015	463	462
Additional paid-in capital	64,287	64,622
Retained earnings	996,253	964,270
Accumulated other comprehensive loss	(196,135 )	(228,861 )
Total stockholders' equity - PRA Group, Inc.	864,868	800,493
Noncontrolling interest	43,874	39,254
Total equity	908,742	839,747
Total liabilities and equity	\$3,268,833	\$2,990,567

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

PRA Group, Inc.  
Consolidated Income Statements  
For the three months ended March 31, 2016 and 2015  
(unaudited)  
(Amounts in thousands, except per share amounts)

	Three Months Ended March 31,	
	2016	2015
Revenues:		
Income recognized on finance receivables, net	\$206,507	\$228,403
Fee income	16,266	13,053
Other revenue	2,109	3,750
Total revenues	224,882	245,206
Operating expenses:		
Compensation and employee services	66,765	65,271
Legal collection fees	12,950	13,691
Legal collection costs	17,182	20,854
Agency fees	10,884	8,261
Outside fees and services	15,808	12,797
Communication	9,882	10,418
Rent and occupancy	3,796	3,560
Depreciation and amortization	6,070	4,610
Other operating expenses	10,651	9,578
Total operating expenses	153,988	149,040
Income from operations	70,894	96,166
Other income and (expense):		
Interest expense	(19,959 )	(14,776 )
Foreign exchange gain/(loss)	(1,850 )	6,789
Income before income taxes	49,085	88,179
Provision for income taxes	16,232	30,044
Net income	32,853	58,135
Adjustment for net income attributable to noncontrolling interest	870	—
Net income attributable to PRA Group, Inc.	\$31,983	\$58,135
Net income per common share attributable to PRA Group, Inc.:		
Basic	\$0.69	\$1.19
Diluted	\$0.69	\$1.19
Weighted average number of shares outstanding:		
Basic	46,243	48,724
Diluted	46,372	49,052

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

PRA Group, Inc.

Consolidated Statements of Comprehensive Income/(Loss)

For the three months ended March 31, 2016 and 2015

(unaudited)

(Amounts in thousands)

	Three Months Ended March 31,	
	2016	2015
Net income	\$32,853	\$58,135
Other comprehensive (loss)/income:		
Change in foreign currency translation	36,694	(62,699 )
Total other comprehensive income/(loss)	69,547	(4,564 )
Comprehensive income attributable to noncontrolling interest:		
Net income attributable to noncontrolling interest	870	—
Change in foreign currency translation	3,968	—
Comprehensive income attributable to noncontrolling interest	4,838	—
Comprehensive income/(loss) attributable to PRA Group, Inc.	\$64,709	\$(4,564 )

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

PRA Group, Inc.

Consolidated Statement of Changes in Equity

For the three months ended March 31, 2016

(unaudited)

(Amounts in thousands)

	Common Stock Shares	Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Noncontrolling Interest	Total Equity
Balance at December 31, 2015	46,173	\$ 462	\$ 64,622	\$ 964,270	\$ (228,861 )	\$ 39,254	\$ 839,747
Components of comprehensive income:							
Net income	—	—	—	31,983	—	870	32,853
Foreign currency translation adjustment	—	—	—	—	32,726	3,968	36,694
Distributions paid to noncontrolling interest	—	—	—	—	—	(218 )	(218 )
Vesting of nonvested shares	155	1	(1 )	—	—	—	—
Amortization of share-based compensation	—	—	3,437	—	—	—	3,437
Tax deficiency from share-based compensation	—	—	(1,339 )	—	—	—	(1,339 )
Employee stock relinquished for payment of taxes	—	—	(2,432 )	—	—	—	(2,432 )
Balance at March 31, 2016	46,328	\$ 463	\$ 64,287	\$ 996,253	\$ (196,135 )	\$ 43,874	\$ 908,742

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

PRA Group, Inc.  
Consolidated Statements of Cash Flows  
For the three months ended March 31, 2016 and 2015  
(unaudited)  
(Amounts in thousands)

	Three Months Ended March 31, 2016	2015
Cash flows from operating activities:		
Net income	\$ 32,853	\$ 58,135
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of share-based compensation	3,437	3,636
Depreciation and amortization	6,070	4,610
Amortization of debt discount and issuance costs	2,746	1,048
Deferred tax expense	4,815	7,617
Net foreign currency transaction loss/(gain)	305	(6,789)
Changes in operating assets and liabilities:		
Other assets	(42,818)	4,201
Other receivables, net	(2,304)	(3,876)
Accounts payable	(1,773)	5,290
Income taxes payable, net	6,412	11,100
Accrued expenses	(6,806)	(21,752)
Other liabilities	9,161	763
Net cash provided by operating activities	12,098	63,983
Cash flows from investing activities:		
Purchases of property and equipment	(6,383)	(3,212)
Acquisition of finance receivables, net of buybacks	(321,594)	(183,828)
Collections applied to principal on finance receivables	177,826	171,344
Business acquisitions, net of cash acquired	(25,018)	—
Purchase of investments	—	(42,705)
Proceeds from sales and maturities of investments	5,568	41,189
Net cash used in investing activities	(169,601)	(17,212)

## Cash flows from financing activities:

Tax (deficiency)/benefit from share-based compensation	(1,339)	)	4,127	
Proceeds from lines of credit	378,706		140,976	
Principal payments on lines of credit	(223,117)	)	(94,044)	)
Repurchases of common stock	—		(77,802)	)
Distributions paid to noncontrolling interest	(218)	)	—	
Principal payments on long-term debt	(5,000)	)	(33,750)	)
Payments of debt issuance costs	(8,477)	)	—	
Net increase in interest-bearing deposits	6,238		7,539	
Net cash provided by/(used in) financing activities	146,793		(52,954)	)
Effect of exchange rate on cash	18,780		7,064	
Net increase in cash and cash equivalents	8,070		881	
Cash and cash equivalents, beginning of period	71,372		39,661	
Cash and cash equivalents, end of period	\$ 79,442		\$ 40,542	
Supplemental disclosure of cash flow information:				
Cash paid for interest	\$ 16,873		\$ 14,376	
Cash paid for income taxes	6,196		7,082	

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



## PRA Group, Inc.

## Notes to Consolidated Financial Statements

## 1. Organization and Business:

Throughout this report, the terms "PRA Group," "our," "we," "us," the "Company," or similar terms refer to PRA Group, Inc. and its subsidiaries.

PRA Group, Inc., a Delaware corporation, along with its subsidiaries, is a financial and business service company operating in the Americas and Europe. The Company's primary business is the purchase, collection and management of portfolios of nonperforming loans. The Company also services receivables on behalf of clients, provides business tax revenue administration, audit, discovery and recovery services for state and local governments in the United States, and provides class action claims settlement recovery services and related payment processing to corporate clients.

The consolidated financial statements of the Company are prepared in accordance with U.S. generally accepted accounting principles ("GAAP") and include the accounts of all of its subsidiaries. All significant intercompany accounts and transactions have been eliminated. Under the guidance of the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 280 "Segment Reporting" ("ASC 280"), the Company has determined that it has several operating segments that meet the aggregation criteria of ASC 280, and, therefore, it has one reportable segment, accounts receivable management, based on similarities among the operating units including the nature of the products and services, the nature of the production processes, the types or class of customer for their products and services, the methods used to distribute their products and services and the nature of the regulatory environment.

The following table shows the amount of revenue generated for the three months ended March 31, 2016 and 2015 and long-lived assets held at March 31, 2016 and 2015 for the United States, the Company's country of domicile, and outside of the United States (amounts in thousands):

	As Of And For The Three Months Ended March 31, 2016		As Of And For The Three Months Ended March 31, 2015	
	Revenues	Long-Lived Assets	Revenues	Long-Lived Assets
United States	\$170,507	\$ 37,316	\$184,671	\$ 37,141
Outside the United States	54,375	10,469	60,535	9,714
Total	\$224,882	\$ 47,785	\$245,206	\$ 46,855

Revenues are attributed to countries based on the location of the related operations. Long-lived assets consist of net property and equipment. The Company reports revenues earned from its debt purchasing and collection activities and its fee-based services. It is impracticable for the Company to report further breakdowns of revenues from external customers by product or service.

The accompanying unaudited consolidated financial statements of the Company have been prepared in accordance with Rule 10-01 of Regulation S-X promulgated by the Securities and Exchange Commission (the "SEC") and, therefore, do not include all information and disclosures required by U.S. GAAP for complete financial statements. In the opinion of the Company, however, the accompanying unaudited consolidated financial statements contain all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the Company's consolidated balance sheet as of March 31, 2016, its consolidated income statements and statements of comprehensive income for the three months ended March 31, 2016 and 2015, its consolidated statement of changes in stockholders' equity for the three months ended March 31, 2016, and its consolidated statements of cash flows for the three months ended March 31, 2016 and 2015. The consolidated income statements of the Company for the three months ended March 31, 2016 may not be indicative of future results. Certain prior period amounts have been reclassified for consistency with the current period presentation. These unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's 2015

Annual Report on Form 10-K, filed on February 26, 2016.

PRA Group, Inc.

Notes to Consolidated Financial Statements

## 2. Finance Receivables, net:

Changes in finance receivables, net for the three months ended March 31, 2016 and 2015 were as follows (amounts in thousands):

	Three Months Ended March 31,	
	2016	2015
Balance at beginning of year	\$2,202,113	\$2,001,790
Acquisitions of finance receivables <sup>(1)</sup>	336,379	183,828
Foreign currency translation adjustment	16,411	(59,502 )
Cash collections	(384,333 )	(399,747 )
Income recognized on finance receivables, net	206,507	228,403
Cash collections applied to principal and net allowance charges/(reversals)	(177,826 )	(171,344 )
Balance at end of year	\$2,377,077	\$1,954,772

(1) Acquisitions of finance receivables are net of buybacks and include certain capitalized acquisition related costs. At the time of acquisition, each pool is estimated based on projected amounts and timing of future cash collections using the proprietary models of the Company.

Based upon current projections, cash collections applied to principal on finance receivables as of March 31, 2016 are estimated to be as follows for the twelve months in the periods ending March 31, (amounts in thousands):

2017	\$626,013
2018	524,122
2019	416,351
2020	320,164
2021	196,566
2022	131,793
2023	72,504
2024	41,693
2025	18,992
2026	14,221
Thereafter	14,658
Total	\$2,377,077

At March 31, 2016, the Company had aggregate net finance receivables balances in pools accounted for under the cost recovery method of \$122.7 million; at December 31, 2015, the amount was \$21.0 million.

Accretable yield represents the amount of income recognized on finance receivables the Company can expect to generate over the remaining life of its existing portfolios based on estimated future cash flows as of the balance sheet date. Additions represent the original expected accretable yield, on portfolios purchased during the period, to be earned by the Company based on its proprietary buying models. Net reclassifications from nonaccretable difference to accretable yield primarily result from the Company's increase in its estimate of future cash flows. When applicable, net reclassifications to nonaccretable difference from accretable yield result from the Company's decrease in its estimates of future cash flows and allowance charges that exceed the Company's increase in its estimate of future cash flows.

PRA Group, Inc.  
Notes to Consolidated Financial Statements

Changes in accretable yield for the three months ended March 31, 2016 and 2015 were as follows (amounts in thousands):

	Three Months Ended March 31,	
	2016	2015
Balance at beginning of year	\$2,727,204	\$2,513,185
Income recognized on finance receivables, net	(206,507 )	(228,403 )
Additions	260,249	172,382
Reclassifications (to)/from nonaccretable difference	(1,035 )	119,252
Foreign currency translation adjustment	99,839	(72,260 )
Balance at end of year	\$2,879,750	\$2,504,156

The following is a summary of activity within the Company's valuation allowance account, all of which relates to loans acquired with deteriorated credit quality, for the three months ended March 31, 2016 and 2015 (amounts in thousands):

	Three Months Ended March 31,	
	2016	2015
Beginning balance	\$114,861	\$86,166
Allowance charges	10,018	2,685
Reversal of previous recorded allowance charges	(120 )	(1,055 )
Net allowance charges	9,898	1,630
Foreign currency translation adjustment	(171 )	—
Ending balance	\$124,588	\$87,796

### 3. Investments:

Investments consist of the following at March 31, 2016 and December 31, 2015 (amounts in thousands):

	March 31, December 31,	
	2016	2015
Available-for-sale		
Securitized assets	\$ 4,686	\$ 4,649
Government bonds and fixed income funds	637	3,405
Held-to-maturity		
Securitized assets	50,566	50,247
Other investments		
Private equity funds	15,524	15,498
Total investments	\$ 71,413	\$ 73,799
Available-for-Sale		

Investments in securitized assets: The Company holds a majority interest in a closed-end Polish investment fund. The fund was formed in December 2014 to acquire portfolios of nonperforming consumer loans in Poland. The Company's investment consists of a 100% interest in the Series B certificates and a 20% interest in the Series C certificates. Each certificate comes with one vote and is governed by a co-investment agreement. Series C certificates, which share equally in the residual profit of the fund, are accounted for as debt securities classified as available-for-sale and are stated at fair value. Income is recognized using the effective yield method. There was no revenue recorded during the three months ended March 31, 2016 and 2015 from this investment.

#### Held-to-Maturity

Investments in securitized assets: The Company holds a majority interest in a closed-end Polish investment fund. The certificates, which provide a preferred return based on the expected net income of the portfolios, are accounted for as a

beneficial interest in securitized financial assets and stated at amortized cost. The Company has determined it has the ability and intent to hold these certificates until maturity, which occurs when the fund terminates or liquidates its assets. The preferred return is not a guaranteed return. Income is recognized under FASB ASC Topic 325-40, "Beneficial Interest in Securitized Financial Assets" ("ASC 325-40"). Income is recognized using the effective yield method. The Company adjusts the yield for changes in

## PRA Group, Inc.

## Notes to Consolidated Financial Statements

estimated cash flows prospectively through earnings. If the fair value of the investment falls below its carrying amount and the decline is deemed to be other than temporary, the investment is written down, with a corresponding charge to earnings. The underlying securities have both known principal repayment terms as well as unknown principal repayments due to potential borrower pre-payments. Accordingly, it is difficult to accurately predict the final maturity date of these investments. Revenues recognized on these investments were \$1.6 million and \$1.2 million during the three months ended March 31, 2016 and 2015, respectively, and are recorded in the Other Revenue line item in the income statement.

## Other Investments

Investments in private equity funds: Investments in private equity funds represent limited partnerships in which the Company has less than a 3% interest and are carried at cost. Distributions received from the partnerships are included in other revenue. Distributions received in excess of the Company's proportionate share of accumulated earnings are applied as a reduction of the cost of the investment. Distributions received from investments carried at cost were \$0.2 million and \$2.1 million during the three months ended March 31, 2016 and 2015, respectively.

The amortized cost and estimated fair value of available-for sale and held-to-maturity investments at March 31, 2016 and December 31, 2015 were as follows (amounts in thousands):

	March 31, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Aggregate Fair Value
Available-for-sale				
Securitized assets	\$5,823	\$ —	—\$ 1,137	\$ 4,686
Government bonds and fixed income funds	637	—	—	637
Held-to-maturity				
Securitized assets	50,566	5,343	—	55,909

	December 31, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Aggregate Fair Value
Available-for-sale				
Securitized assets	\$5,855	\$ —	—\$ 1,206	\$ 4,649
Government bonds and fixed income funds	3,405	—	—	3,405
Held-to-maturity				
Securitized assets	50,247	5,366	—	55,613

## 4. Borrowings:

The Company's borrowings consisted of the following as of the dates indicated (amounts in thousands):

	March 31, 2016	December 31, 2015
Domestic and Canadian revolving credit	\$543,998	\$541,799
Term loan	165,000	170,000
Note payable	169,938	169,938
Multicurrency revolving credit	758,293	576,433
Convertible senior notes	287,500	287,500
Less: Debt discount and issuance costs	(28,305)	(28,541)
Total	\$1,896,424	\$1,717,129

Domestic and Canadian Revolving Credit and Term Loan

On December 19, 2012, the Company entered into a credit facility with Bank of America, N.A., as administrative agent, and a syndicate of lenders named therein (such agreement as later amended or modified, the "Credit Agreement"). On March 24, 2016, the Company entered into a Loan Modification Agreement and Seventh Amendment (the "Seventh Amendment") to the Credit Agreement which (a) extended the maturity date of loans and commitments under the Credit Agreement in an aggregate principal

PRA Group, Inc.  
Notes to Consolidated Financial Statements

amount of approximately \$745.9 million, including a \$23.0 million net increase in the commitments of the extending lenders, to the earlier of December 21, 2020 (the "Notes") or 91 days prior to the maturity of the Company's 3.00% Convertible Senior Notes due August 1, 2020, (b) modified the accordion feature under the Credit Agreement to allow the Company to request from new and existing lenders up to an additional \$125.0 million in loans and commitments under the Credit Agreement, (c) increased the credit given in the domestic borrowing base for estimated remaining collections of eligible asset pools, (d) increased the baskets available for permitted investments, equity repurchases and redemptions of the Company's convertible notes, and (e) increased the maximum total leverage ratio of the Company and its subsidiaries to 2.25 to 1.0.

The total credit facility under the Credit Agreement includes an aggregate principal amount of \$963.0 million (subject to compliance with a borrowing base and applicable debt covenants), which consists of (i) a fully-funded \$165.0 million term loan, (ii) a \$748.0 million domestic revolving credit facility, and (iii) a \$50 million Canadian revolving credit facility. The Company's domestic revolving credit facility includes an optional increase in commitments for a \$20 million swingline loan sublimit and a \$125.0 million accordion feature, and also provides for up to \$20 million of letters of credit that would reduce amounts available for borrowing. The facility matures on the earlier of December 21, 2020 or 91 days prior to the maturity of the Notes. The term and revolving loans accrue interest, at the option of the Company, at either the base rate or the Eurodollar rate (as defined in the Credit Agreement) for the applicable term plus 2.50% per annum in the case of the Eurodollar rate loans and 1.50% in the case of the base rate loans. The base rate is the highest of (a) the Federal Funds Rate (as defined in the Credit Agreement) plus 0.50%, (b) Bank of America's prime rate, and (c) the Eurodollar rate plus 1.00%. As of March 31, 2016, after taking into account borrowing base restrictions, the Company could have borrowed up to \$219.0 million on the domestic revolving credit facility and up to \$1.9 million on the Canadian revolving credit facility.

The Credit Agreement is secured by a first priority lien on substantially all of the Company's assets. The Credit Agreement, as amended and modified, contains restrictive covenants and events of default including the following:

- borrowings may not exceed 35% of the ERC of all eligible asset pools plus 75% of eligible accounts receivable;
- the consolidated leverage ratio (as defined in the Credit Agreement) cannot exceed 2.25 to 1.0 as of the end of any fiscal quarter;
- consolidated capital expenditures during any fiscal year cannot exceed \$40 million;
- cash dividends and distributions during any fiscal year cannot exceed \$20 million;
- stock repurchases during any fiscal year cannot exceed \$100 million plus 50% of the prior year's net income;
- permitted acquisitions (as defined in the Credit Agreement) during any fiscal year cannot exceed \$250 million;
- indebtedness in the form of senior, unsecured convertible notes or other unsecured financings cannot exceed \$500 million in the aggregate (without respect to the Company's 3.00% Convertible Senior Notes due 2020);
- the Company must maintain positive consolidated income from operations (as defined in the Credit Agreement) during any fiscal quarter; and
- restrictions on changes in control.

The revolving credit facility also bears an unused line fee of 0.375% per annum, payable quarterly in arrears.

The Company's borrowings on this credit facility at March 31, 2016 consisted of \$165.0 million outstanding on the term loan with an annual interest rate as of March 31, 2016 of 2.93% and \$544.0 million outstanding on the revolving facilities with a weighted average interest rate of 2.98%. At December 31, 2015, the Company's borrowings on this credit facility consisted of \$170.0 million outstanding on the term loan with an annual interest rate as of December 31, 2015 of 2.92% and \$541.8 million outstanding on the revolving facility with a weighted average interest rate of 2.89%.

#### Note Payable

In conjunction with the closing of the Aktiv Kapital AS ("Aktiv") business acquisition on July 16, 2014, the Company entered into a \$169.9 million promissory note with an affiliate of the seller. On December 30, 2015, the Company exercised its option to extend the maturity date of the promissory note to July 19, 2016. The promissory note bears



interest at the three-month London Interbank Offered Rate ("LIBOR") plus 3.75%. The quarterly interest due can be paid or added into the promissory note balance at the Company's option. At March 31, 2016, the balance due on the note was \$169.9 million with an annual interest rate of 4.38%.

**Multicurrency Revolving Credit Facility**

On October 23, 2014, the Company entered into a credit agreement with DNB Bank ASA for a Multicurrency Revolving Credit Facility (such agreement as later amended or modified, "the Multicurrency Revolving Credit Agreement"). On February 19, 2016, the Company entered into a Second Amendment to the Multicurrency Revolving Credit Agreement which provided for, (i) the extension of the final repayment date to February 19, 2021, (ii) an increase to the total commitments from \$750 million to

PRA Group, Inc.

Notes to Consolidated Financial Statements

\$900 million, subject to certain requirements, and (iii) an ERC ratio (as defined in Multicurrency Revolving Credit Agreement) ranging from 32.2% to 38.7% depending on the mix of portfolios owned, subject to the payment of additional associated fees.

Under the terms of the Multicurrency Revolving Credit Agreement, the credit facility includes an aggregate amount of \$900 million, of which \$168.8 million is available to be drawn (subject to the borrowing base), accrues interest at the Interbank Offered Rate ("IBOR") plus 2.50-3.30% (as determined by the ERC Ratio as defined in the Multicurrency Revolving Credit Agreement), bears an unused line fee of 35% of the margin, currently 1.05% per annum, payable monthly in arrears, and matures on February 19, 2021. The Multicurrency Revolving Credit Agreement also includes an Overdraft Facility aggregate amount of \$40 million, of which \$12.9 million is available to be drawn (subject to the borrowing base), accrues interest (per currency) at the daily rates as published by the facility agent, bears a facility line fee of 0.125% per annum, payable quarterly in arrears, and also matures February 19, 2021.

The Multicurrency Revolving Credit Agreement is secured by i) the shares of most of the Company's European subsidiaries and ii) all intercompany loan receivables in Europe. The Multicurrency Revolving Credit Agreement also contains restrictive covenants and events of default including the following:

- the ERC Ratio (as defined in the Multicurrency Revolving Credit Agreement) in Europe can range from 32.2% to 38.7% depending on the mix of portfolios owned, subject to the payment of additional associated fees;
- the GIBD Ratio (as defined in the Multicurrency Revolving Credit Agreement) in Europe cannot exceed 3.0 to 1.0 as of the end of any fiscal quarter;
- interest bearing deposits in AK Nordic AB cannot exceed SEK 500,000,000;
- cash collections must exceed 95% of Europe's ERC for the same set of portfolios, measured monthly on a quarterly basis.

At March 31, 2016, the balance on the Multicurrency Revolving Credit Agreement was \$758.3 million, with a weighted average annual interest rate of 3.86%. At December 31, 2015, the balance on the Multicurrency Revolving Credit Agreement was \$576.4 million, with a weighted average annual interest rate of 3.64%.

Convertible Senior Notes

On August 13, 2013, the Company completed the private offering of \$287.5 million in aggregate principal amount of the Notes. The Notes were issued pursuant to an Indenture, dated August 13, 2013 (the "Indenture") between the Company and Wells Fargo Bank, National Association, as trustee. The Indenture contains customary terms and covenants, including certain events of default after which the Notes may be due and payable immediately. The Notes are senior unsecured obligations of the Company and mature on August 1, 2020. Interest on the Notes is payable semi-annually, in arrears, on February 1 and August 1 of each year. Prior to February 1, 2020, the Notes will be convertible only upon the occurrence of specified events. On or after February 1, 2020, the Notes will be convertible at any time. Upon conversion, the Notes may be settled, at the Company's option, in cash, shares of the Company's common stock, or any combination thereof. Holders of the Notes have the right to require the Company to repurchase all or some of their Notes at 100% of their principal amount, plus any accrued and unpaid interest, upon the occurrence of a fundamental change (as defined in the Indenture). In addition, upon the occurrence of a make-whole fundamental change (as defined in the Indenture), the Company may, under certain circumstances, be required to increase the conversion rate for the Notes converted in connection with such a make-whole fundamental change. The conversion rate for the Notes is initially 15.2172 shares per \$1,000 principal amount of Notes, which is equivalent to an initial conversion price of approximately \$65.72 per share of the Company's common stock, and is subject to adjustment in certain circumstances pursuant to the Indenture. The Company does not have the right to redeem the Notes prior to maturity. As of March 31, 2016, none of the conditions allowing holders of the Notes to convert their Notes had occurred.

As noted above, upon conversion, holders of the Notes will receive cash, shares of the Company's common stock or a combination of cash and shares of the Company's common stock, at the Company's election. However, the Company's current intent is to settle conversions through combination settlement (i.e., the Notes would be converted into cash up

to the aggregate principal amount, and shares of the Company's common stock or a combination of cash and shares of the Company's common stock, at the Company's election, would be used to settle the remainder). As a result, and in accordance with authoritative guidance related to derivatives and hedging and earnings per share, only the conversion spread is included in the diluted earnings per share calculation, if dilutive. Under such method, the settlement of the conversion spread has a dilutive effect when the average share price of the Company's common stock during any quarter exceeds \$65.72.

The Company determined that the fair value of the Notes at the date of issuance was approximately \$255.3 million, and designated the residual value of approximately \$32.2 million as the equity component. Additionally, the Company allocated approximately \$7.3 million of the \$8.2 million original Notes issuance cost as debt issuance cost and the remaining \$0.9 million as equity issuance cost.

## PRA Group, Inc.

## Notes to Consolidated Financial Statements

FASB ASC 470-20, "Debt with Conversion and Other Options" ("ASC 470-20"), requires that, for convertible debt instruments that may be settled fully or partially in cash upon conversion, issuers must separately account for the liability and equity components in a manner that will reflect the entity's nonconvertible debt borrowing rate when interest cost is recognized in subsequent periods. Additionally, debt issuance costs are required to be allocated in proportion to the allocation of the liability and equity components and accounted for as debt issuance costs and equity issuance costs, respectively.

The balances of the liability and equity components of the Notes outstanding were as follows as of the dates indicated (amounts in thousands):

	March 31, 2016	December 31, 2015
Liability component - principal amount	\$287,500	\$287,500
Unamortized debt discount	(21,302 )	(22,402 )
Liability component - net carrying amount	\$266,198	\$265,098
Equity component	\$31,306	\$31,306

The debt discount is being amortized into interest expense over the remaining life of the Notes using the effective interest rate, which is 4.92%.

Interest expense related to the Notes was as follows for the periods indicated (amounts in thousands):

	Three Months Ended March 31, 2016	2015
Interest expense - stated coupon rate	\$2,156	\$2,156
Interest expense - amortization of debt discount	1,100	1,048
Total interest expense - convertible senior notes	\$3,256	\$3,204

The Company believes it was in compliance with all covenants under its financing arrangements as of March 31, 2016 and December 31, 2015.

The following principal payments are due on the Company's borrowings as of March 31, 2016 for the twelve month periods ending March 31, (amounts in thousands):

2017	\$194,938
2018	176,901
2019	10,000
2020	10,000
2021	1,532,890
Total	\$1,924,729

#### 5. Property and Equipment, net:

Property and equipment, at cost, consisted of the following as of the dates indicated (amounts in thousands):

	March 31, 2016	December 31, 2015
Software	\$65,211	\$62,198
Computer equipment	21,994	21,109
Furniture and fixtures	14,896	11,888
Equipment	13,242	12,874
Leasehold improvements	14,884	15,112
Building and improvements	7,251	7,235
Land	1,296	1,296
Accumulated depreciation and amortization	(90,989 )	(86,318 )

Property and equipment, net	\$47,785	\$45,394
-----------------------------	----------	----------

14

---

PRA Group, Inc.  
Notes to Consolidated Financial Statements

Depreciation and amortization expense relating to property and equipment for the three months ended March 31, 2016 and 2015, was \$4.3 million and \$3.8 million, respectively.

6. Goodwill and Intangible Assets, net:

In connection with the Company's business acquisitions, the Company acquired certain tangible and intangible assets. Intangible assets resulting from these acquisitions include client and customer relationships, non-compete agreements, trademarks and technology. Pursuant to ASC 350, the Company performs an annual review of goodwill on October 1 or more frequently if indicators of impairment exist. The Company performed an annual review of goodwill as of October 1, 2015, and concluded that no goodwill impairment was necessary.

At March 31, 2016 and 2015, the carrying value of goodwill was \$524.9 million and \$496.7 million, respectively. The goodwill acquired during the three months ended March 31, 2016 is deductible for U.S. income tax purposes. The following table represents the changes in goodwill for the three months ended March 31, 2016 and 2015 (amounts in thousands):

	Three Months Ended March 31,	
	2016	2015
Balance at beginning of period:		
Goodwill	\$501,553	\$533,842
Accumulated impairment loss	(6,397 )	(6,397 )
	495,156	527,445
Changes:		
Acquisitions <sup>(1)</sup>	4,742	—
Foreign currency translation adjustment	24,972	(30,792 )
Net change in goodwill	29,714	(30,792 )
Goodwill	531,267	503,050
Accumulated impairment loss	(6,397 )	(6,397 )
Balance at end of period:	\$524,870	\$496,653

(1) The \$4.7 million addition to goodwill during the three months ended March 31, 2016, is mainly attributable to the acquisition of Recovery Management Systems Corporation ("RMSC") in addition to a purchase price adjustment from a previous acquisition.

7. Share-Based Compensation:

The Company has an Omnibus Incentive Plan (the "Plan") to assist the Company in attracting and retaining selected individuals to serve as employees and directors, who are expected to contribute to the Company's success and to achieve long-term objectives that will benefit stockholders of the Company. The Plan enables the Company to award shares of the Company's common stock to select employees and directors, as described in the Plan, not to exceed 5.4 million shares, as authorized by the Plan.

Total share-based compensation expense was \$3.4 million and \$3.6 million for the three months ended March 31, 2016 and 2015, respectively. Tax benefits resulting from tax deductions in excess of share-based compensation expense (windfall tax benefits) recognized under the provisions of FASB ASC Topic 718 "Compensation-Stock Compensation" ("ASC 718") are credited to additional paid-in capital in the Company's Consolidated Balance Sheets. Realized tax shortfalls, if any, are first offset against the cumulative balance of windfall tax benefits, if any, and then charged directly to income tax expense. The total tax benefit realized from share-based compensation was approximately \$2.4 million and \$7.5 million for the three months ended March 31, 2016 and 2015, respectively.

Nonvested Shares

As of March 31, 2016, total future compensation costs related to nonvested share awards (not including nonvested shares granted under the Long-Term Incentive ("LTI") Program) is estimated to be \$11.2 million with a weighted

average remaining life for all nonvested shares of 2.0 years (not including nonvested shares granted under the LTI program). With the exception of the awards made pursuant to the LTI program and a few employee and director grants, the nonvested shares vest ratably over three to five years and are expensed over their vesting period.

## PRA Group, Inc.

## Notes to Consolidated Financial Statements

The following summarizes all nonvested share transactions, excluding those related to the LTI program, from December 31, 2014 through March 31, 2016 (share amounts in thousands):

	Nonvested Shares Outstanding	Weighted-Average Price at Grant Date
December 31, 2014	339	\$ 47.34
Granted	100	53.29
Vested	(151 )	42.15
Canceled	(4 )	47.49
December 31, 2015	284	52.20
Granted	148	29.01
Vested	(78 )	44.31
Canceled	(27 )	57.96
March 31, 2016	327	\$ 43.08

The total grant date fair value of shares vested during the three months ended March 31, 2016 and 2015 was \$3.4 million and \$2.8 million, respectively.

## Long-Term Incentive Program

Pursuant to the Plan, the Compensation Committee may grant time-vested and performance based nonvested shares. All shares granted under the LTI program were granted to key employees of the Company.

The following summarizes all LTI program share transactions from December 31, 2014 through March 31, 2016 (share amounts in thousands):

	Nonvested LTI Shares Outstanding	Weighted-Average Price at Grant Date
December 31, 2014	488	\$ 30.52
Granted at target level	132	52.47
Adjustments for actual performance	122	34.59
Vested	(252 )	20.21
Canceled	(7 )	40.05
December 31, 2015	483	42.80
Granted at target level	240	28.98
Adjustments for actual performance	(67 )	34.59
Vested	(177 )	34.59
Canceled	(14 )	55.07
March 31, 2016	465	\$ 39.59

The total grant date fair value of shares vested during the three months ended March 31, 2016 and 2015 was \$6.1 million and \$5.1 million, respectively.

At March 31, 2016, total future compensation expenses, assuming the current estimated performance levels are achieved, related to nonvested share awards granted under the LTI program are estimated to be approximately \$13.3 million. The Company assumed a 7.5% forfeiture rate for these grants and the remaining shares have a weighted average life of 1.8 years at March 31, 2016.

## 8. Income Taxes:

The Company follows the guidance of FASB ASC Topic 740 "Income Taxes" ("ASC 740") as it relates to the provision for income taxes and uncertainty in income taxes. The guidance prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return.



For tax purposes, the Company utilizes the cost recovery method of accounting. Under the cost recovery method, collections on finance receivables are applied first to principal to reduce the finance receivables to zero before taxable income is recognized.

PRA Group, Inc.  
Notes to Consolidated Financial Statements

The Internal Revenue Service ("IRS") examined the Company's 2005 through 2012 tax returns and has asserted that tax revenue recognition using the cost recovery method does not clearly reflect taxable income. The Company believes it has sufficient support for the technical merits of its position, and believes cost recovery to be an acceptable tax revenue recognition method for the Company's industry. The Company has received Notices of Deficiency for tax years ended December 31, 2005 through 2012. The proposed deficiencies relate to the cost recovery method of tax accounting. In response to the notices, the Company filed petitions in the U.S. Tax Court (the "Tax Court") challenging the deficiencies. On July 10, 2015 and July 21, 2015, the IRS filed Motions for Summary Judgment for tax years 2008 through 2012 and 2005 through 2007, respectively. On November 12, 2015 the Tax Court denied the IRS's Motions for Summary Judgment and set this matter for trial to begin on September 19, 2016.

If the Company is unsuccessful in the Tax Court and any potential appeals, it may be required to pay the related deferred taxes, and possibly interest and penalties. At March 31, 2016 and December 31, 2015, deferred tax liabilities related to this matter were \$252.3 million and \$251.7 million, respectively. Any adverse determination on this matter could result in the Company amending state tax returns for prior years, increasing its taxable income in those states. The Company files tax returns in multiple state jurisdictions; therefore, any underpayment of state tax will accrue interest in accordance with the respective state statute. At March 31, 2016 and December 31, 2015, the Company's estimate of the potential federal and state interest was \$95.2 million and \$91.0 million, respectively.

ASC 740 requires the recognition of interest if the tax law would require interest to be paid on the underpayment of taxes, and recognition of penalties if a tax position does not meet the minimum statutory threshold to avoid payment of penalties. The Company believes it has sufficient support for the technical merits of its position and that it is more likely than not this position will be sustained. Accordingly, the Company has not accrued for interest or penalties. At March 31, 2016, the tax years subject to examination by the major federal, state and international taxing jurisdictions are 2003, 2005 and subsequent years. The 2003 tax year remains open to examination because of a net operating loss that originated in that year but was not fully utilized until the 2005 tax year. The examination periods for the 2005 through 2012 tax years are suspended until a decision of the Tax Court becomes final.

The Company intends for predominantly all foreign earnings to be permanently reinvested in its foreign operations. If foreign earnings were repatriated, the Company would need to accrue and pay taxes, although foreign tax credits may be available to partially reduce U.S. income taxes. The amount of cash on hand related to foreign operations with permanently reinvested earnings was \$56.9 million and \$51.5 million as of March 31, 2016 and December 31, 2015, respectively.

#### 9. Earnings per Share:

Basic earnings per share ("EPS") are computed by dividing net income available to common stockholders of PRA Group, Inc. by weighted average common shares outstanding. Diluted EPS are computed using the same components as basic EPS with the denominator adjusted for the dilutive effect of the Notes and nonvested share awards, if dilutive. For the Notes, only the conversion spread is included in the diluted earnings per share calculation, if dilutive. Under such method, the settlement of the conversion spread has a dilutive effect when the average share price of the Company's common stock during any quarter exceeds \$65.72, which did not occur during the period from which the Notes were issued on August 13, 2013 through March 31, 2016. Share-based awards that are contingent upon the attainment of performance goals are not included in the computation of diluted EPS until the performance goals have been attained. The dilutive effect of nonvested shares is computed using the treasury stock method, which assumes any proceeds that could be obtained upon the vesting of nonvested shares would be used to purchase common shares at the average market price for the period. The assumed proceeds include the windfall tax benefit that would be realized upon assumed exercise.

The following table provides a reconciliation between the computation of basic EPS and diluted EPS for the three months ended March 31, 2016 and 2015 (amounts in thousands, except per share amounts):

For the Three Months Ended March 31,	
2016	2015

Edgar Filing: PRA GROUP INC - Form 10-Q

	Net income attributable to PRA Group, Inc.	Weighted Average Common Shares	EPS	Net income attributable to PRA Group, Inc.	Weighted Average Common Shares	EPS
Basic EPS	\$31,983	46,243	\$0.69	\$58,135	48,724	\$1.19
Dilutive effect of nonvested share awards		129	—		328	—
Diluted EPS	\$31,983	46,372	\$0.69	\$58,135	49,052	\$1.19

There were no antidilutive options outstanding for the three months ended March 31, 2016 and 2015.

PRA Group, Inc.  
Notes to Consolidated Financial Statements

10. Commitments and Contingencies:

Employment Agreements:

The Company has entered into employment agreements, most of which expire on December 31, 2017, with all of its U.S. executive officers and with several members of its U.S. senior management group. Such agreements provide for base salary payments as well as bonuses that are based on the attainment of specific management goals. At March 31, 2016, estimated future compensation under these agreements is approximately \$16.5 million. The agreements also contain confidentiality and non-compete provisions. Outside the United States, employment agreements are in place with employees pursuant to local country regulations. Generally, these agreements do not have expiration dates and therefore it is impractical to estimate the amount of future compensation under these agreements. Accordingly, the future compensation under these agreements is not included in the \$16.5 million total above.

Leases:

The Company is party to various operating leases with respect to its facilities and equipment. The future minimum lease payments at March 31, 2016 total approximately \$59.2 million.

Forward Flow Agreements:

The Company is party to several forward flow agreements that allow for the purchase of nonperforming loans at pre-established prices. The maximum remaining amount to be purchased under forward flow agreements at March 31, 2016 is approximately \$477.3 million.

Finance Receivables:

Certain agreements for the purchase of finance receivables portfolios contain provisions that may, in limited circumstances, require the Company to refund a portion or all of the collections subsequently received by the Company on particular accounts. The potential refunds as of the balance sheet date are not considered to be significant.

Litigation and Regulatory Matters:

The Company is from time to time subject to routine legal claims, proceedings and regulatory matters, most of which are incidental to the ordinary course of its business. The Company initiates lawsuits against customers and is occasionally countersued by them in such actions. Also, customers, either individually, as members of a class action, or through a governmental entity on behalf of customers, may initiate litigation against the Company in which they allege that the Company has violated a state or federal law in the process of collecting on an account. From time to time, other types of lawsuits are brought against the Company. Additionally, the Company receives subpoenas and other requests or demands for information from regulators or governmental authorities who are investigating the Company's debt collection activities. The Company evaluates and responds appropriately to such requests.

The Company accrues for potential liability arising from legal proceedings and regulatory matters when it is probable that such liability has been incurred and the amount of the loss can be reasonably estimated. This determination is based upon currently available information for those proceedings in which the Company is involved, taking into account the Company's best estimate of such losses for those cases for which such estimates can be made. The Company's estimate involves significant judgment, given the varying stages of the proceedings (including the fact that many of them are currently in preliminary stages), the number of unresolved issues in many of the proceedings (including issues regarding class certification and the scope of many of the claims), and the related uncertainty of the potential outcomes of these proceedings. In making determinations of the likely outcome of pending litigation, the Company considers many factors, including, but not limited to, the nature of the claims, the Company's experience with similar types of claims, the jurisdiction in which the matter is filed, input from outside legal counsel, the likelihood of resolving the matter through alternative mechanisms, the matter's current status and the damages sought or demands made. Accordingly, the Company's estimate will change from time to time, and actual losses could be more than the current estimate.

The Company believes that the estimate of the aggregate range of reasonably possible losses in excess of the amount accrued for its legal proceedings outstanding at March 31, 2016, excluding the potential interest associated with the

IRS matter described below, is from \$0 to \$82 million.

In certain legal proceedings, the Company may have recourse to insurance or third-party contractual indemnities to cover all or portions of its litigation expenses, judgments, or settlements. Loss estimates and accruals for potential liability related to legal proceedings are typically exclusive of potential recoveries, if any, under the Company's insurance policies or third-party

PRA Group, Inc.  
Notes to Consolidated Financial Statements

indemnities. The Company has not recorded any potential recoveries under the Company's insurance policies or third-party indemnities, with the exception of the Telephone Consumer Protection Act Litigation matter.

The matters described below fall outside of the normal parameters of the Company's routine legal proceedings.

Telephone Consumer Protection Act Litigation

The Company has been named as defendant in a number of putative class action cases, each alleging that the Company violated the Telephone Consumer Protection Act ("TCPA") by calling consumers' cellular telephones without their prior express consent. On December 21, 2011, the U.S. Judicial Panel on Multi-District Litigation entered an order transferring these matters into one consolidated proceeding in the U.S. District Court for the Southern District of California (the "Court"). On November 14, 2012, the putative class plaintiffs filed their amended consolidated complaint in the matter, now styled as *In re Portfolio Recovery Associates, LLC Telephone Consumer Protection Act Litigation*, case No. 11-md-02295 (the "MDL action"). Following the ruling of the U.S. Federal Communications Commission on June 10, 2015 on various petitions concerning the TCPA, the Court lifted the stay of these matters that had been in place since May 20, 2014. In January 2016, the parties reached a settlement agreement in principle under which the parties have agreed to seek court approval of class certification and the proposed settlement. In April 2016, the parties sought preliminary Court approval of a settlement agreement, whereby the Company would pay \$18 million to resolve the MDL action. The Company had fully accrued for the settlement amount as of December 31, 2015.

Internal Revenue Service Audit

The IRS examined the Company's 2005 through 2012 tax returns and has asserted that tax revenue recognition using the cost recovery method does not clearly reflect taxable income. The Company believes it has sufficient support for the technical merits of its position, and believes cost recovery to be an acceptable tax revenue recognition method for the Company's industry. The Company has received Notices of Deficiency for tax years ended December 31, 2005 through 2012. The proposed deficiencies relate to the cost recovery method of tax accounting for finance receivables. In response to the notices, the Company filed petitions in the Tax Court challenging the deficiencies. On July 10, 2015 and July 21, 2015, the IRS filed Motions for Summary Judgment for tax years 2008 through 2012 and 2005 through 2007, respectively. On November 12, 2015, the Tax Court denied the IRS's Motions for Summary Judgment and set this matter for trial to begin on September 19, 2016. If the Company is unsuccessful in the Tax Court and any potential appeals, it may ultimately be required to pay the related deferred taxes, and possibly interest and penalties. Deferred tax liabilities related to this matter were \$252.3 million at March 31, 2016. Any adverse determination on this matter could result in the Company amending state tax returns for prior years, increasing its taxable income in those states. The Company files tax returns in multiple state jurisdictions; therefore, any underpayment of state tax will accrue interest in accordance with the respective state statute. The Company's estimate of the potential federal and state interest is \$95.2 million as of March 31, 2016, which has not been accrued.

Portfolio Recovery Associates, LLC v. Guadalupe Mejia

On May 11, 2015, an unfavorable jury verdict was delivered against the Company in a matter pending in Jackson County, Missouri. The jury awarded Guadalupe Mejia \$251,000 in compensatory damages and \$82,009,549 in punitive damages for her counter-claim against the Company, alleging malicious prosecution and impermissible collection practices. The Company believes the verdict and magnitude of the Award to be erroneous and appealed the award. Unless overturned or significantly reduced, the award could result in a loss of up to the amount of the jury award.

11. Fair Value:

As defined by FASB ASC Topic 820, "Fair Value Measurements and Disclosures" ("ASC 820"), fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820 also requires the consideration of differing levels of inputs in the determination of fair values.

Those levels of input are summarized as follows:

Level 1: Quoted prices in active markets for identical assets and liabilities.

Level 2: Observable inputs other than Level 1 quoted prices, such as quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3: Unobservable inputs that are supported by little or no market activity. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar

PRA Group, Inc.  
Notes to Consolidated Financial Statements

techniques as well as instruments for which the determination of fair value requires significant management judgment or estimation.

The level in the fair value hierarchy within which a fair value measurement in its entirety falls is based on the lowest level input that is significant to the fair value measurement in its entirety.

Financial Instruments Not Required To Be Carried at Fair Value

In accordance with the disclosure requirements of FASB ASC Topic 825, "Financial Instruments" ("ASC 825"), the table below summarizes fair value estimates for the Company's financial instruments not required to be carried at fair value. The total of the fair value calculations presented does not represent, and should not be construed to represent, the underlying value of the Company.

The carrying amounts of the financial instruments in the following table are recorded in the consolidated balance sheets at March 31, 2016 and December 31, 2015 (amounts in thousands):

	March 31, 2016		December 31, 2015	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets:				
Cash and cash equivalents	\$79,442	\$ 79,442	\$71,372	\$ 71,372
Held-to-maturity investments	50,566	55,909	50,247	55,613
Other investments	15,524	16,420	15,498	16,803
Finance receivables, net	2,377,072	2,807,600	2,202,113	3,704,432
Financial liabilities:				
Interest-bearing deposits	55,349	55,349	46,991	46,991
Revolving lines of credit	1,302,291	1,302,291	1,118,232	1,118,232
Term loans	165,000	165,000	170,000	170,000
Notes and loans payable	169,938	169,938	169,938	169,938
Convertible senior notes	266,198	228,701	265,098	241,126

Disclosure of the estimated fair values of financial instruments often requires the use of estimates. The carrying amount and estimates of the fair value of the Company's debt obligations outlined above do not include any related debt issuance costs associated with the debt obligations. The Company uses the following methods and assumptions to estimate the fair value of the financial instruments in the above table:

Cash and cash equivalents: The carrying amount approximates fair value and quoted prices for identical assets can be found in active markets. Accordingly, the Company estimates the fair value of cash and cash equivalents using Level 1 inputs.

Held-to-maturity investments: Fair value of the Company's investment in Series B certificates of a closed-end Polish investment fund is estimated using proprietary pricing models that the Company utilizes to make portfolio purchase decisions. Accordingly, the Company estimates the fair value of its held-to-maturity investments using Level 3 inputs as there is little observable market data available and management is required to use significant judgment in its estimates.

Other investments: This class of investments consists of private equity funds that invest primarily in loans and securities including single-family residential debt; corporate debt products; and financially-oriented, real-estate-rich and other operating companies in the Americas, Western Europe, and Japan. These investments are subject to certain restrictions regarding transfers and withdrawals. The investments can never be redeemed with the funds. Instead, the nature of the investments in this class is that distributions are received through the liquidation of the underlying assets of the fund. The fair value of the Company's interest is valued by the fund managers; accordingly, the Company estimates the fair value of these investments using Level 3 inputs. The investments are expected to be returned through distributions as a result of liquidations of the funds' underlying assets over 1 to 4 years.



Finance receivables, net: The Company records purchased receivables at cost, which represents a significant discount from the contractual receivable balances due. The Company computed the estimated fair value of these receivables using proprietary pricing models that the Company utilizes to make portfolio purchase decisions. Accordingly, the Company's fair value estimates use Level 3 inputs as there is little observable market data available and management is required to use significant judgment in its estimates.

## PRA Group, Inc.

## Notes to Consolidated Financial Statements

Interest-bearing deposits: The carrying amount approximates fair value due to the short-term nature of the deposits and the observable quoted prices for similar instruments in active markets. Accordingly, the Company uses Level 2 inputs for its fair value estimates.

Revolving lines of credit: The carrying amount approximates fair value due to the short-term nature of the interest rate periods and the observable quoted prices for similar instruments in active markets. Accordingly, the Company uses Level 2 inputs for its fair value estimates.

Term loans: The carrying amount approximates fair value due to the short-term nature of the interest rate periods and the observable quoted prices for similar instruments in active markets. Accordingly, the Company uses Level 2 inputs for its fair value estimates.

Notes and loans payable: The carrying amount approximates fair value due to the short-term nature of the loan terms and the observable quoted prices for similar instruments in active markets. Accordingly, the Company uses Level 2 inputs for its fair value estimates.

Convertible notes: The Notes are carried at historical cost, adjusted for the debt discount. The fair value estimates for these Notes incorporates quoted market prices which were obtained from secondary market broker quotes which were derived from a variety of inputs including client orders, information from their pricing vendors, modeling software, and actual trading prices when they occur. Accordingly, the Company uses Level 2 inputs for its fair value estimates.

#### Financial Instruments Required To Be Carried At Fair Value

The carrying amounts in the following table are measured at fair value on a recurring basis in the accompanying consolidated balance sheets at March 31, 2016 and December 31, 2015 (amounts in thousands):

Fair Value Measurements as of March 31, 2016				
	Level 1	Level 2	Level 3	Total
Assets:				
Available-for-sale investments	\$637	\$	—\$4,686	\$5,323
Liabilities:				
Interest rate swap contracts (recorded in accrued expenses)	—	3,309	—	3,309

Fair Value Measurements as of December 31, 2015				
	Level 1	Level 2	Level 3	Total
Assets:				
Available-for-sale investments	\$3,405	\$	—\$4,649	\$8,054
Liabilities:				
Interest rate swap contracts (recorded in accrued expenses)	—	1,601	—	1,601

Available-for-sale investments: Fair value of the Company's investment in Series C certificates of a closed-end Polish investment fund is estimated using proprietary pricing models that the Company utilizes to make portfolio purchase decisions. Accordingly, the Company estimates the fair value of its available-for-sale investments using Level 3 inputs as there is little observable market data available and management is required to use significant judgment in its estimates.

Interest rate swap contracts: The interest rate swap contracts are carried at fair value which is determined by using industry standard valuation models. These models project future cash flows and discount the future amounts to a present value using market-based observable inputs, including interest rate curves and other factors. Accordingly, the Company uses Level 2 inputs for its fair value estimates.

#### 12. Recent Accounting Pronouncements:

In May 2014, FASB issued Accounting Standards Update ("ASU") 2014-09, "Revenue from Contracts with Customers" ("ASU 2014-09") that updates the principles for recognizing revenue. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2014-09 also amends the required disclosures of the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. ASU 2014-09 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017, and can be

PRA Group, Inc.  
Notes to Consolidated Financial Statements

adopted either retrospectively to each prior reporting period presented or as a cumulative-effect adjustment as of the date of adoption, with early application not permitted. The Company is evaluating its implementation approach and the potential impacts of the new standard on its existing revenue recognition policies and procedures.

In June 2014, FASB issued ASU 2014-12, "Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period" ("ASU 2014-12"). ASU 2014-12 requires that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. As such, the performance target should not be reflected in estimating the grant-date fair value of the award. ASU 2014-12 is effective for annual reporting periods beginning after December 15, 2015, with early adoption permitted. The Company adopted ASU 2014-12 in the first quarter of 2016 which had no material impact on the Company's Consolidated Financial Statements.

In February 2015, FASB issued ASU 2015-02, "Consolidation (Topic 810), Amendments to the Consolidation Analysis" ("ASU 2015-02"). The amendments under the new guidance modify the evaluation of whether limited partnerships and similar legal entities are variable interest entities ("VIEs") or voting interest entities and eliminate the presumption that a general partner should consolidate a limited partnership. ASU 2015-02 is effective for public business entities for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted, including adoption in an interim period. A reporting entity also may apply the amendments retrospectively. The Company adopted ASU 2015-02 in the first quarter of 2016 which had no material impact on the Company's Consolidated Financial Statements.

In April 2015, FASB issued ASU 2015-03, "Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs" ("ASU 2015-03"). ASU 2015-03 requires an entity to present debt issuance costs related to a recognized debt liability in the balance sheet as a direct deduction from the carrying amount of the debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this update. For public business entities, this update is effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. An entity should apply the new guidance on a retrospective basis. The Company retrospectively adopted ASU 2015-03 in the first quarter of 2016. Upon adoption, the Company reclassified its debt issuance costs from "Other assets" to "Borrowings" in its Consolidated Balance Sheets which did not have a material impact on the Company's Consolidated Financial Statements.

In April 2015, FASB issued ASU 2015-05, "Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement" ("ASU 2015-05"). ASU 2015-05 provides explicit guidance to help companies evaluate the accounting for fees paid by a customer in a cloud computing arrangement. The new guidance clarifies that if a cloud computing arrangement includes a software license, the customer should account for the license consistent with its accounting for other software licenses. If the arrangement does not include a software license, the customer should account for the arrangement as a service contract. For public business entities, this update is effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. An entity can elect to adopt the new guidance either prospectively for all arrangements entered into or materially modified after the effective date, or on a retrospective basis. The Company prospectively adopted ASU 2015-05 in the first quarter of 2016 which had no material impact on the Company's Consolidated Financial Statements.

In February 2016, FASB issued ASU 2016-02, "Leases (Topic 842) Section A-Leases: Amendments to the FASB Account Standards Codification" ("ASU 2016-02"). The amendments under the new guidance increases transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet for those leases classified as operating leases under previous generally accepted accounting principles. ASU 2016-02 requires that a lessee should recognize a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term on the balance sheet. It is effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years, using a modified retrospective

approach and early adoption is permitted. The Company is currently in the process of evaluating the impact of adoption of the ASU on its consolidated financial statements.

In March 2016, FASB issued ASU 2016-09, "Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting" ("ASU 2016-09"). The amendments under the new guidance simplifies several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. ASU 2016-09 is effective for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years and early adoption is permitted. The Company is currently in the process of evaluating the impact of adoption of the ASU on its consolidated financial statements.

PRA Group, Inc.  
Notes to Consolidated Financial Statements

13. Subsequent Event:

On April 26, 2016, the Company successfully completed its public tender offer to purchase shares of DTP S.A., a Poland-based debt collection company (“DTP”). As of April 26, 2016, 99.73% of the outstanding shares in DTP had been tendered at PLN 4.90 per share (approximately US \$1.26 per share), for an aggregate purchase price of PLN 174.5 million (approximately US \$45.0 million). The Company has received all approvals and has filed all notices required for the completion of the tender offer. The Company intends to purchase all the remaining shares of DTP through Polish regulatory procedures and will then initiate the process to withdraw DTP's shares from public trading and delist the company from the Warsaw Stock Exchange.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

### Forward-Looking Statements:

This report contains forward-looking statements within the meaning of the federal securities laws. These forward-looking statements involve risks, uncertainties and assumptions that, if they never materialize or prove incorrect, could cause our results to differ materially from those expressed or implied by such forward-looking statements. All statements, other than statements of historical fact, are forward-looking statements, including statements regarding overall cash collection trends, gross margin trends, operating cost trends, liquidity and capital needs and other statements of expectations, beliefs, future plans and strategies, anticipated events or trends, and similar expressions concerning matters that are not historical facts. The risks, uncertainties and assumptions referred to above may include the following:

- changes in the credit or capital markets, which affect our ability to borrow money or raise capital;
- a prolonged economic recovery or a deterioration in the economic or inflationary environment in North America or Europe, including the interest rate environment;
- our ability to replace our nonperforming loans with additional receivables portfolios;
- our ability to purchase nonperforming loans at appropriate prices;
- our reliance on third-party vendors having procedures and controls which are compliant or error free;
- our ability to obtain accurate and authentic account documents relating to accounts that we acquire and the possibility that documents that we provide could contain errors;
- our ability to collect sufficient amounts on our nonperforming loans;
- our ability to successfully acquire receivables of new asset types;
- changes in, or interpretations of, bankruptcy or collection laws that could negatively affect our business, including by causing an increase in certain types of bankruptcy filings involving liquidations, which may cause our collections to decrease;
- changes in, or interpretations of, federal, state, local, or foreign laws or the administrative practices of various bankruptcy courts, which may impact our ability to collect on our nonperforming loans;
- our ability to obtain adequate insurance coverage at reasonable prices;
- our ability to manage risks associated with our international operations;
- changes in tax laws regarding earnings of our subsidiaries located outside of the United States ("U.S.");
- the possibility that we could incur goodwill or other intangible asset impairment charges;
- our ability to retain members of our senior management team;
- the possibility that our U.S. work force could become unionized in the future, which could adversely affect the stability of our production and increase our costs;
- the imposition of additional taxes on us;
- the possibility that we could incur significant allowance charges on our finance receivables;
- our loss contingency accruals may not be adequate to cover actual losses;
- the possibility that class action suits and other litigation could divert our management's attention and increase our expenses;
- adverse outcomes in pending litigation;
- the possibility that we could incur business to technology disruptions or cyber incidents;
- the degree, nature, and resources of our competition;
- the possibility that new business acquisitions prove unsuccessful or strain or divert our resources;
- the potential effects of threatened or actual terrorism and war;
- our ability to compete in markets where we do business;
- our ability to manage growth successfully or to successfully integrate our growth strategy;
- the possibility that we or our industry could experience negative publicity or reputational attacks;
- the possibility that a sudden collapse of one of the financial institutions in which we are depositors could negatively affect our financial results;
- our ability to collect and enforce our finance receivables may be limited under federal, state, and foreign laws;

our ability to adjust to debt collection and debt-buying regulations that may be promulgated by the Consumer Financial Protection Bureau ("CFPB") and the regulatory and enforcement activities of the CFPB;  
our ability to comply with existing and new regulations of the collection industry, the failure of which could result in penalties, fines, litigation, damage to our reputation, or the suspension or termination of or required modification to our ability to conduct our business;  
changes in accounting standards, governmental laws and regulations or the manner in which they are interpreted or applied which could increase our costs and liabilities or impact our operations;  
investigations or enforcement actions by governmental authorities, which could result in changes to our business practices; negatively impact our portfolio purchasing volume; make collection of account balances more difficult or expose us to the risk of fines, penalties, restitution payments, and litigation;



the possibility that compliance with foreign and U.S. laws and regulations that apply to our international operations could increase our cost of doing business in international jurisdictions;

net capital requirements pursuant to the European Union Capital Requirements Directive ("CRD IV"), which could impede the business operations of our subsidiaries;

our ability to maintain, renegotiate or replace our credit facility;

our ability to satisfy the restrictive covenants in our debt agreements;

the possibility that the accounting for convertible debt securities could have an adverse effect on our financial results;

our ability to raise the funds necessary to repurchase the convertible senior notes or to settle conversions in cash;

the possibility that conversion of the convertible senior notes could affect the price of our common stock;

changes in interest or exchange rates, which could reduce our net income, and the possibility that future hedging strategies may not be successful, which could adversely affect our results of operations and financial condition, as could our failure to comply with hedge accounting principles and interpretations; and

the risk factors listed from time to time in our filings with the Securities and Exchange Commission (the "SEC").

You should assume that the information appearing in this Quarterly Report on Form 10-Q (this "Quarterly Report") is accurate only as of the date it was issued. Our business, financial condition, results of operations and prospects may have changed since that date.

For a discussion of the risks, uncertainties and assumptions that could affect our future events, developments or results, you should carefully review the following "Management's Discussion and Analysis of Financial Condition and Results of Operations," the "Risk Factors" contained in Part II, Item 1A of this Quarterly Report, as well as the discussion of "Business" and "Risk Factors" described in Part I, Item I and Item 1A of our 2015 Annual Report on Form 10-K, filed on February 26, 2016.

Our forward-looking statements could be wrong in light of these and other risks, uncertainties and assumptions. The future events, developments or results described in this report could turn out to be materially different. Except as required by law, we assume no obligation to publicly update or revise our forward-looking statements after the date of this report and you should not expect us to do so.

Investors should also be aware that while we do, from time to time, communicate with securities analysts and others, we do not, by policy, selectively disclose to them any material nonpublic information or other confidential commercial information. Accordingly, stockholders should not assume that we agree with any statement or report issued by any analyst regardless of the content of the statement or report. We do not, by policy, confirm forecasts or projections issued by others. Thus, to the extent that reports issued by securities analysts contain any projections, forecasts or opinions, such reports are not our responsibility.

#### Frequently Used Terms

We use the following terminology throughout this document:

- "Allowance charges" refers to a reduction in income recognized on finance receivables on pools of finance receivables whose cash collection estimates were below expectations or are projected to be below expectations.
- "Amortization rate" refers to cash collections applied to principal on finance receivables as a percentage of total cash collections.
- "Buybacks" refers to purchase price refunded by the seller due to the return of ineligible accounts.
- "Cash collections" refers to collections on our owned finance receivables portfolios.
- "Cash receipts" refers to collections on our owned finance receivables portfolios plus fee income.
- "Core" accounts or portfolios refer to accounts or portfolios that are nonperforming loans and are not in an insolvent status upon purchase. These accounts are aggregated separately from insolvency accounts.
- "Estimated remaining collections" or "ERC" refers to the sum of all future projected cash collections on our owned finance receivables portfolios.
- "Fee income" refers to revenues generated from our fee-for-service businesses.
- "Income recognized on finance receivables" refers to income derived from our owned finance receivables portfolios.
- "Income recognized on finance receivables, net" refers to income derived from our owned finance receivables portfolios and is shown net of allowance charges/reversals.
-

"Insolvency" accounts or portfolios refer to accounts or portfolios of receivables that are in an insolvent status when we purchase them and as such are purchased as a pool of insolvent accounts. These include Individual Voluntary Arrangements ("IVAs"), Trust Deeds in the United Kingdom, Consumer Proposals in Canada and bankruptcy accounts in the United States, Canada and the United Kingdom.

"Net finance receivable balance" is recorded on our balance sheet and refers to the purchase price less principal amortization and net allowance charges/reversals.

- "Principal amortization" refers to cash collections applied to principal on finance receivables.

"Purchase price" refers to the cash paid to a seller to acquire nonperforming loans, plus certain capitalized costs, less buybacks.

- "Purchase price multiple" refers to the total estimated collections (as defined below) on owned finance receivables portfolios divided by purchase price.

- "Total estimated collections" refers to actual cash collections, including cash sales, plus estimated remaining collections on our finance receivables portfolios.

All references in this Quarterly Report to the "PRA Group," "our," "we," "us," the "Company" or similar terms are to PRA Group, Inc. and its subsidiaries.

#### Overview

We are a global financial and business services company with operations in the Americas and Europe. Our primary business is the purchase, collection and management of portfolios of nonperforming loans. We also service receivables on behalf of clients on either a commission or transaction-fee basis, provide class action claims settlement recovery services and related payment processing to corporate clients, and provide vehicle location, skip tracing and collateral recovery services for auto lenders, governments and law enforcement.

We are headquartered in Norfolk, Virginia, and as of March 31, 2016 employ 3,748 full time equivalents. Our shares of common stock are traded on the NASDAQ Global Select Market under the symbol "PRAA."

Our industry is highly regulated under various laws. In the United States they include the Fair Debt Collection Practices Act, Fair Credit Reporting Act, Dodd-Frank Act, Telephone Consumer Protection Act and its prohibition against unfair, deceptive and abusive acts and practices and other federal and state laws. Likewise, our business is regulated by various laws in the European countries and Canadian territories in which we operate. Any finding or adjudication that we have failed to comply with applicable laws or regulations could subject the Company to penalties, litigation losses and expenses, damage to our reputation, or the suspension or termination of or required modification to our ability to conduct collections, which would adversely affect our financial results and condition. Specifically in the U.S., the CFPB continues to look into practices regarding the collection of consumer debt and is expected to adopt additional rules that will affect our industry.

#### Earnings Summary

During the three months ended March 31, 2016, net income attributable to PRA Group, Inc. was \$32.0 million, or \$0.69 per diluted share, compared with \$58.1 million, or \$1.19 per diluted share, in the three months ended March 31, 2015. Total revenues decreased 8.3% to \$224.9 million in the three months ended March 31, 2016, compared to the three months ended March 31, 2015. Revenues in the three months ended March 31, 2016 consisted of \$206.5 million in income recognized on finance receivables, net, \$16.3 million in fee income and \$2.1 million in other revenue.

Income recognized on finance receivables, net, in the three months ended March 31, 2016 decreased \$21.9 million, or 9.6%, over the three months ended March 31, 2015, primarily as a result of an \$8.3 million increase in net allowance charges and a \$15.4 million decrease in cash collections. During the three months ended March 31, 2016, we incurred \$9.9 million in net allowance charges, compared with \$1.6 million in the three months ended March 31, 2015. Our finance receivables amortization rate, including net allowance charges/reversals, was 46.3% for the three months ended March 31, 2016 compared to 42.9% for the three months ended March 31, 2015. Our finance receivables amortization rate, excluding net allowance charges/reversals, was 43.7% for the three months ended March 31, 2016 compared to 42.5% for the three months ended March 31, 2015. Cash collections, which drive our finance receivable income, were \$384.3 million in the three months ended March 31, 2016, down 3.9%, or \$15.4 million, as compared to the three months ended March 31, 2015.

Fee income increased to \$16.3 million during the three months ended March 31, 2016 from \$13.1 million in the three months ended March 31, 2015, primarily due to an increase in fee income by PRA Location Services, LLC ("PLS") and the fee income generated by our newly acquired Insolvency business, RMSC, which we acquired in the first quarter of 2016. This was offset by a decrease in fee income from PRA Europe which is due primarily to a decline in the amount of contingent fee work provided to us by debt owners.

A summary of the sources of our revenue during the three months ended March 31, 2016 and 2015 is presented below (amounts in thousands):

	For the Three Months Ended March 31,	
	2016	2015
Cash collections	\$384,333	\$399,747
Amortization of investment	(167,928 )	(169,714 )
Net allowance charges	(9,898 )	(1,630 )
Income recognized on finance receivables, net	206,507	228,403
Fee income	16,266	13,053
Other revenue	2,109	3,750
Total revenues	\$224,882	\$245,206

Operating expenses were \$154.0 million for the three months ended March 31, 2016, an increase of \$5.0 million or 3.4%, as compared to the three months ended March 31, 2015.

During the three months ended March 31, 2016 and 2015, we acquired finance receivables portfolios at an approximate cost of \$336.8 million and \$185.0 million, respectively. In any period, we acquire nonperforming loans that can vary dramatically in their age, type and ultimate collectability. We may pay significantly different purchase rates for purchased receivables within any period as a result of this quality fluctuation. In addition, market forces can drive pricing rates up or down in any period, irrespective of other quality fluctuations. As a result, the average purchase rate paid for any given period can fluctuate dramatically based on our particular buying activity in that period. However, regardless of the average purchase price and for similar time frames, we intend to target a similar internal rate of return, after direct expenses, in pricing our portfolio acquisitions during any quarter; therefore, the absolute rate paid is not necessarily relevant to the estimated profitability of a period's buying.

## Results of Operations

The results of operations include the financial results of the Company and all of our subsidiaries. The following table sets forth certain operating data as a percentage of total revenues for the periods indicated:

For the Three  
Months Ended  
March 31,  
2016      2015

## Revenues:

Income recognized on finance receivables, net	91.8	%	93.2	%
Fee income	7.2	%	5.3	%
Other revenue	1.0	%	1.5	%
Total revenues	100.0	%	100.0	%

## Operating expenses:

Compensation and employee services	29.7	%	26.6	%
Legal collection fees	5.8	%	5.6	%
Legal collection costs	7.6	%	8.5	%
Agency fees	4.8	%	3.4	%
Outside fees and services	7.0	%	5.2	%
Communication	4.4	%	4.2	%
Rent and occupancy	1.7	%	1.5	%
Depreciation and amortization	2.7	%	1.9	%
Other operating expenses	4.7	%	3.9	%
Total operating expenses	68.5	%	60.8	%
Income from operations	31.5	%	39.2	%

## Other income and (expense):

Interest expense	(8.9)	)%	(6.0)	)%
Foreign exchange gain/(loss)	(0.8)	)%	2.8	%
Income before income taxes	21.8	%	36.0	%
Provision for income taxes	7.2	%	12.3	%
Net income	14.6	%	23.7	%
Adjustment for net income attributable to noncontrolling interest	0.4	%	—	%
Net income attributable to PRA Group, Inc.	14.2	%	23.7	%

Three Months Ended March 31, 2016 Compared To Three Months Ended March 31, 2015

## Revenues

Total revenues were \$224.9 million for the three months ended March 31, 2016, a decrease of \$20.3 million, or 8.3%, compared to total revenues of \$245.2 million for the three months ended March 31, 2015.

## Income Recognized on Finance Receivables, net

Income recognized on finance receivables, net was \$206.5 million for the three months ended March 31, 2016, a decrease of \$21.9 million, or 9.6%, compared to income recognized on finance receivables, net, of \$228.4 million for the three months ended March 31, 2015. The decrease was primarily the result of an \$8.3 million increase in net allowance charges and a \$15.4 million decrease in cash collections. During the three months ended March 31, 2016, we incurred \$9.9 million in net allowance charges, compared with \$1.6 million in the three months ended March 31, 2015. Our finance receivables amortization rate, including net allowance charges/reversals, was 46.3% for the three months ended March 31, 2016 compared to 42.9% for the three months ended March 31, 2015. Our finance receivables amortization rate, excluding net allowance charges/reversals, was 43.7% for the three months ended March 31, 2016 compared to 42.5% for the three months ended March 31, 2015. Cash collections, which drive our finance receivable income, were \$384.3 million in the three months ended March 31, 2016, down \$15.4 million, or 3.9%, as compared to the three months ended March 31, 2015.



Accretable yield represents the amount of income recognized on finance receivables the Company can expect to generate over the remaining life of its existing portfolios based on estimated future cash flows as of the balance sheet date. Additions represent the original expected accretable yield on portfolios purchased during the period to be earned by the Company based on its proprietary buying models. Net reclassifications from nonaccretable difference to accretable yield primarily result from the Company's increase in its estimate of future cash flows. Increases in future cash flows may occur as portfolios age and actual cash collections exceed those originally expected. If those cash flows are determined to be incremental to the portfolio's original forecast, future projections of cash flows are generally increased resulting in higher expected revenue and hence increases in accretable yield. During the three months ended March 31, 2016, the Company reclassified \$1.0 million to nonaccretable difference from accretable yield primarily due to a decrease in cash collection forecasts. When applicable, net reclassifications to nonaccretable difference from accretable yield result from the Company's decrease in its estimates of future cash flows and allowance charges that exceed the Company's increase in its estimate of future cash flows. During the three months ended March 31, 2015, the Company reclassified \$119.3 million from nonaccretable difference to accretable yield primarily due to increased cash collection forecasts relating to pools acquired from 2007-2013.

Income recognized on finance receivables, net, is shown net of changes in valuation allowances which are recorded for significant decreases in expected cash flows or a change in timing of cash flows which would otherwise require a reduction in the stated yield on a pool of accounts. For the three months ended March 31, 2016, we recorded net allowance charges of \$9.9 million. On our domestic Core portfolios, we recorded net allowance charges of \$7.1 million on portfolios purchased mainly in 2012 and 2013. On our Insolvency portfolios, we recorded allowance charges of \$0.3 million on our domestic portfolios. We also recorded allowance charges of \$2.2 million on our European portfolios, and \$0.3 million on our Canadian portfolios.

For the three months ended March 31, 2015, we recorded net allowance charges of \$1.6 million. On our domestic Core portfolios, we recorded allowance reversals of \$0.8 million on portfolios purchased between 2006 and 2008, offset by allowance charges of \$2.7 million on portfolios purchased between 2010 and 2012. On our Insolvency portfolios, we recorded allowance reversals of \$0.3 million on our domestic portfolios. No allowance charges or reversals were recorded during the period on the portfolios purchased in Europe.

In any given period, we may be required to record valuation allowances due to pools of receivables underperforming our previous expectations. Factors that may contribute to the recording of valuation allowances may include both internal as well as external factors. External factors which may have an impact on the collectability, and subsequently to the overall profitability, of purchased pools of nonperforming loans include new laws or regulations relating to collections, new interpretations of existing laws or regulations, and the overall condition of the economy. Internal factors which may have an impact on the collectability, and subsequently the overall profitability, of purchased pools of nonperforming loans would include necessary revisions to initial and post-acquisition scoring and modeling estimates, operational activities (relating to the collection and movement of accounts on both our collection floor and external channels), and changes in productivity related to turnover and retention of our collection staff.

#### Fee Income

Fee income increased to \$16.3 million in the three months ended March 31, 2016 from \$13.1 million in the three months ended March 31, 2015, primarily due to an increase in fee income by PLS, the fee income generated by our newly acquired Insolvency business, RMSC, which we acquired in the first quarter of 2016, and the fee income generated by RCB Investimentos S.A. ("RCB"), which we acquired in the third quarter of 2015. This was partially offset by a decrease in fee income generated by our foreign operations.

#### Other Revenue

Other revenue decreased to \$2.1 million in the three months ended March 31, 2016 from \$3.8 million in the three months ended March 31, 2015, primarily due to a decrease in revenue generated by our investments.

#### Operating Expenses

Operating expenses were \$154.0 million for the three months ended March 31, 2016, an increase of \$5.0 million or 3.4% compared to operating expenses of \$149.0 million for the three months ended March 31, 2015. This increase was primarily due to an increase in corporate legal expenses, which are included in "Outside fees and services" in our consolidated income statements, and an increase in agency fees. Operating expenses were 38.4% of cash receipts for

the three months ended March 31, 2016 compared to 36.1% for the three months ended March 31, 2015.



### Compensation and Employee Services

Compensation and employee services expenses were \$66.8 million for the three months ended March 31, 2016, an increase of \$1.5 million, or 2.3%, compared to compensation and employee services expenses of \$65.3 million for the three months ended March 31, 2015. The increase in compensation and employee services expenses was mainly due to the expansion of our professional staff in our information technology, finance and compliance departments. Total full-time equivalents decreased 2.6% to 3,748 as of March 31, 2016, down from 3,847 as of March 31, 2015.

Compensation and employee services expenses as a percentage of cash receipts increased to 16.7% for the three months ended March 31, 2016, from 15.8% of cash receipts for the three months ended March 31, 2015.

### Legal Collection Fees

Legal collection fees represent contingent fees incurred for the cash collections generated by our independent third party collection attorneys. Legal collection fees were \$13.0 million for the three months ended March 31, 2016, compared to legal collection fees of \$13.7 million for the three months ended March 31, 2015. The decrease is attributable to a decrease in external legal cash collections. Legal collection fees were 3.2% of cash receipts for the three months ended March 31, 2016 compared to 3.3% of cash receipts for the three months ended March 31, 2015.

### Legal Collection Costs

Legal collection costs consist of costs paid to courts where a lawsuit is filed and the cost of documents received from sellers of nonperforming loans. Legal collection costs were \$17.2 million for the three months ended March 31, 2016, a decrease of \$3.7 million, or 17.7%, compared to legal collection costs of \$20.9 million for the three months ended March 31, 2015. Between 2012 and 2015, we expanded the number of accounts brought into the legal collection process resulting in increased legal collections costs. This expansion has subsided over the last several quarters which led to the decrease in the current period. Legal collection costs for the three months ended March 31, 2016 were 4.3% of cash receipts, compared to 5.1% for the three months ended March 31, 2015.

### Agency Fees

Agency fees primarily represent third party collection fees and costs paid to repossession agents to repossess vehicles. Agency fees were \$10.9 million for the three months ended March 31, 2016, compared to \$8.3 million for the three months ended March 31, 2015. This increase was mainly attributable to third-party collection fees incurred by our international operations where we may utilize third party agencies.

### Outside Fees and Services

Outside fees and services expenses were \$15.8 million for the three months ended March 31, 2016, an increase of \$3.0 million, or 23.4%, compared to outside fees and services expenses of \$12.8 million for the three months ended March 31, 2015. This increase was primarily due to a \$1.8 million increase in corporate legal expenses.

### Communication

Communication expenses were \$9.9 million for the three months ended March 31, 2016, compared to communication expenses of \$10.4 million for the three months ended March 31, 2015. None of the decrease was attributable to any significant identifiable items.

### Rent and Occupancy

Rent and occupancy expenses were \$3.8 million for the three months ended March 31, 2016, an increase of \$0.2 million, or 5.6%, compared to rent and occupancy expenses of \$3.6 million for the three months ended March 31, 2015. The increase was primarily due to additional rental expenses incurred as a result of the expansion of our headquarters in Norfolk, Virginia.

### Depreciation and Amortization

Depreciation and amortization expenses were \$6.1 million for the three months ended March 31, 2016, an increase of \$1.5 million, or 32.6%, compared to depreciation and amortization expenses of \$4.6 million for the three months ended March 31, 2015. The increase was primarily due to the amortization expense incurred on intangible assets acquired in connection with the acquisition of RCB.

#### Other Operating Expenses

Other operating expenses were \$10.7 million for the three months ended March 31, 2016, an increase of \$1.1 million, or 11.5%, compared to other operating expenses of \$9.6 million for the three months ended March 31, 2015. None of the increase was attributable to any significant identifiable items.

#### Interest Expense

Interest expense was \$20.0 million during the three months ended March 31, 2016, an increase of \$5.2 million or 35.1%, compared to \$14.8 million for the three months ended March 31, 2015. The increase was primarily due to an increase in average borrowing during the three months ended March 31, 2016 compared to the three months ended March 31, 2015.

#### Net Foreign Currency Transaction Gain/(Loss)

Net foreign currency transaction losses were \$1.9 million for the three months ended March 31, 2016 compared to a net foreign currency transaction gain of \$6.8 million for the three months ended March 31, 2015. In any given period, our foreign entities conduct operations in currencies different from their functional currency which generate foreign currency transaction gains and losses.

#### Provision for Income Taxes

Provision for income taxes was \$16.2 million for the three months ended March 31, 2016, a decrease of \$13.8 million, or 46.0%, compared to provision for income taxes of \$30.0 million for the three months ended March 31, 2015. The decrease is primarily due to a 44.3% decrease in income before taxes for the three months ended March 31, 2016, compared to the three months ended March 31, 2015. During the three months ended March 31, 2016, our effective tax rate was 33.1%, compared to 34.1% for the three months ended March 31, 2015. The decrease in the effective tax rate was due primarily to the combination of projected taxable income between various tax jurisdictions and tax differences driven by foreign exchange.

We intend for predominantly all foreign earnings to be permanently reinvested in our foreign operations. If foreign earnings were repatriated, we would need to accrue and pay taxes, although foreign tax credits may be available to partially reduce U.S. income taxes. The amount of cash on hand related to foreign operations with permanently reinvested earnings was \$56.9 million and \$15.8 million as of March 31, 2016 and 2015, respectively.

#### Supplemental Performance Data

##### Finance Receivables Portfolio Performance

The following tables show certain data related to our finance receivables portfolio. These tables describe the purchase price, actual cash collections and future estimates of cash collections, income recognized on finance receivables (gross and net of allowance charges/(reversals)), principal amortization, allowance charges/(reversals), net finance receivable balances, and the ratio of total estimated collections to purchase price (which we refer to as purchase price multiple) as well as the original purchase price multiple. Certain adjustments, as noted in the footnotes to these tables, have been made to reduce the impact of foreign currency fluctuations on purchase price multiples.

Further, these tables disclose our Americas and European Core and Insolvency portfolios. The accounts represented in the Insolvency tables are those portfolios of accounts that were in an insolvency status at the time of purchase. This contrasts with accounts in our Core portfolios that file for bankruptcy/insolvency protection after we purchase them, which continue to be tracked in their corresponding Core portfolio. Core customers sometimes file for bankruptcy/insolvency protection subsequent to our purchase of the related Core portfolio. When this occurs, we adjust our collection practices accordingly to comply with bankruptcy/insolvency rules and procedures; however, for accounting purposes, these accounts remain in the related Core portfolio. Conversely, Insolvency accounts may be dismissed voluntarily or involuntarily subsequent to our purchase of the related Insolvency portfolio. Dismissal occurs when the terms of the bankruptcy are not met by the petitioner. When this occurs, we are typically free to pursue collection outside of bankruptcy procedures; however, for accounting purposes, these accounts remain in the related Insolvency pool.

Purchase price multiples can vary over time due to a variety of factors including pricing competition, supply levels, age of the receivables purchased, and changes in our operational efficiency. For example, increased pricing competition during the 2005 to 2008 period negatively impacted purchase price multiples of our Core portfolio compared to prior years. Conversely, during the 2009 to 2011 period, pricing disruptions occurred as a result of the

economic downturn. This created unique and advantageous purchasing opportunities, particularly within the Insolvency market, relative to the prior four years.

Purchase price multiples can also vary among types of finance receivables. For example, we incur lower collection costs on our Insolvency portfolio compared with our Core portfolio. This allows us, in general, to pay more for an Insolvency portfolio and experience lower purchase price multiples, while generating similar internal rates of return, net of expenses, when compared with a Core portfolio.

When competition increases and/or supply decreases, pricing often becomes negatively impacted relative to expected collections, and yields tend to trend lower. The opposite tends to occur when competition decreases and/or supply increases.

Within a given portfolio type, to the extent that lower purchase price multiples are the result of more competitive pricing and lower yields, this will generally lead to higher amortization rates and lower profitability. As portfolio pricing becomes more favorable on a relative basis, our profitability will tend to increase. Profitability within given Core portfolio types may also be impacted by the age and quality of the receivables, which impact the cost to collect those accounts.

The numbers presented in the following tables represent gross cash collections and do not reflect any costs to collect; therefore, they may not represent relative profitability. We continue to make enhancements to our analytical abilities, with the intent to collect more cash at a lower cost. To the extent we can improve our collection operations by collecting additional cash from a discrete quantity and quality of accounts, and/or by collecting cash at a lower cost structure, we can positively impact profitability.

Revenue recognition under FASB ASC Topic 310-30, "Loans and Debt Securities Acquired with Deteriorated Credit Quality" ("ASC 310-30") is driven by estimates of total collections as well as the timing of those collections. We record new portfolio purchases based on our best estimate of the cash flows expected at acquisition, which reflects the uncertainties inherent in the purchase of past due loans and the results of our underwriting process. Subsequent to the initial booking, as we gain collection experience and confidence with a pool of accounts, we continuously update ERC. These processes, along with the aforementioned operational enhancements, have tended to cause the ratio of ERC to purchase price for any given year of buying to gradually increase over time. As a result, our estimate of total collections has often increased as pools have aged. Thus, all factors being equal in terms of pricing, one would typically tend to see a higher collection to purchase price ratio from a pool of accounts that was six years from purchase than say a pool that was just two years from purchase.

Due to all the factors described above, readers should be cautious when making comparisons of purchase price multiples among periods and between types of receivables.

## Multiples Tables

Amounts in thousands

Purchase Period	Purchase Price <sup>(3)</sup>	Net Finance Receivables <sup>(4)</sup>	ERC-Historical Period Exchange Rates <sup>(5)</sup>	Total Estimated Collections <sup>(6)</sup>	ERC-Current Period Exchange Rates <sup>(7)</sup>	Current Purchase Price Multiple	Original Purchase Price Multiple <sup>(2)</sup>
Americas-Core							
1996 - 2005	\$368,600	\$3,514	\$20,648	\$1,407,506	\$20,648	382 %	250 %
2006	90,038	4,229	10,856	198,310	10,856	220 %	225 %
2007	179,835	11,315	38,486	449,949	38,486	250 %	227 %
2008	166,506	12,301	32,961	380,049	32,961	228 %	220 %
2009	125,175	4,436	51,659	458,205	51,659	366 %	252 %
2010	148,265	12,172	81,944	536,167	81,944	362 %	247 %
2011	209,815	27,378	130,665	717,248	130,665	342 %	245 %
2012	254,750	65,907	211,192	703,907	211,192	276 %	226 %
2013	391,734	159,717	459,598	1,041,168	459,598	266 %	211 %
2014 <sup>(1)</sup>	406,542	219,935	601,140	1,004,928	594,785	247 %	204 %
2015	448,100	364,544	752,867	933,419	754,232	208 %	205 %
2016 YTD	139,312	135,961	256,384	265,039	256,384	190 %	190 %
Subtotal	2,928,672	1,021,409	2,648,400	8,095,895	2,643,410		
Americas-Insolvency							
2004 - 2005	36,770	4	202	58,626	202	159 %	148 %
2006	17,627	38	389	32,458	389	184 %	139 %
2007	78,524	248	1,064	106,493	1,064	136 %	150 %
2008	108,579	1,016	2,190	169,509	2,190	156 %	163 %
2009	156,001	—	8,964	474,280	8,964	304 %	214 %
2010	209,107	243	13,324	551,490	13,324	264 %	184 %
2011	181,275	8,865	23,650	365,181	23,650	201 %	155 %
2012	251,975	37,166	63,567	375,690	63,567	149 %	136 %
2013	228,158	71,083	104,160	338,278	104,160	148 %	133 %
2014	149,153	75,570	103,325	203,132	103,175	136 %	124 %
2015	65,074	60,821	73,149	80,534	73,149	124 %	125 %
2016 YTD	24,194	23,208	28,032	29,201	28,032	121 %	121 %
Subtotal	1,506,437	278,262	422,016	2,784,872	421,866		
Total Americas	4,435,109	1,299,671	3,070,416	10,880,767	3,065,276		
Europe-Core							
2012	20,459	115	659	31,537	582	154 %	187 %
2013	20,371	1,749	3,236	22,248	2,805	109 %	119 %
2014 <sup>(1)</sup>	798,397	508,614	1,417,932	1,976,007	1,276,871	247 %	208 %
2015	424,056	364,378	590,674	663,675	580,461	157 %	160 %
2016 YTD	176,053	175,599	291,684	292,499	291,684	166 %	166 %
Subtotal	1,439,336	1,050,455	2,304,185	2,985,966	2,152,403		
Europe-Insolvency							
2014	10,880	5,900	11,335	17,047	10,564	157 %	129 %
2015	19,594	15,826	23,592	27,534	22,635	141 %	139 %
2016 YTD	5,233	5,225	7,739	7,800	7,739	149 %	149 %
Subtotal	35,707	26,951	42,666	52,381	40,938		
Total Europe	1,475,043	1,077,406	2,346,851	3,038,347	2,193,341		

Total PRA Group \$5,910,152 \$2,377,077 \$ 5,417,267 \$13,919,114 \$ 5,258,617

(1) The amount reflected in the Purchase Price column includes the acquisition date finance receivable portfolios in Canada and Europe that were acquired in connection with the Aktiv acquisition.

(2) The Original Purchase Price multiple represents the initial full year purchase price multiple in the year of acquisition.

(3) For our international amounts, purchase price is presented at the exchange rate at the end of the quarter in which the portfolio was purchased. In addition, any purchase price adjustments that occur throughout the life of the pool are presented at the period end exchange rate for the respective quarter of purchase.

(4) For our international amounts, Net Finance Receivables are presented at the March 31, 2016 exchange rate.

(5) For our international amounts, ERC-Historical Period Exchange Rates is presented at the period end exchange rate for the respective quarter of purchase.

(6) For our international amounts, Total Estimated Collections is presented at the period end exchange rate for the respective quarter of purchase.

(7) For our international amounts, ERC-Current Period Exchange Rates is presented at the March 31, 2016 exchange rate.

## Portfolio Financial Information

Amounts in thousands

Purchase Period	Purchase Price <sup>(3)</sup>	Cash Collections <sup>(2)</sup>	Gross Revenue <sup>(2)</sup>	Amortization <sup>(2)</sup>	Allowance <sup>(2)</sup>	Net Revenue <sup>(2)</sup>	Net Finance Receivables <sup>(4)</sup>
Americas-Core							
1996 - 2005	\$368,600	\$ 2,914	\$ 2,547	\$ 367	\$ 125	\$ 2,422	\$ 3,514
2006	90,038	811	487	324	—	487	4,229
2007	179,835	2,824	1,991	833	125	1,866	11,315
2008	166,506	2,767	1,692	1,075	—	1,692	12,301
2009	125,175	4,920	3,818	1,102	—	3,818	4,436
2010	148,265	7,652	5,817	1,835	—	5,817	12,172
2011	209,815	14,937	11,713	3,224	400	11,313	27,378
2012	254,750	18,760	13,629	5,131	600	13,029	65,907
2013	391,734	38,082	26,903	11,179	5,850	21,053	159,717
2014 <sup>(1)</sup>	406,542	53,834	32,499	21,335	188	32,311	219,935
2015	448,100	63,520	31,001	32,519	98	30,903	364,544
2016 YTD	139,312	8,550	5,242	3,308	—	5,242	135,961
Subtotal	2,928,672	219,571	137,339	82,232	7,386	129,953	1,021,409
Americas-Insolvency							
2004 - 2005	36,770	19	9	10	—	9	4
2006	17,627	37	20	17	(20)	) 40	38
2007	78,524	84	37	47	(100)	) 137	248
2008	108,579	213	70	143	—	70	1,016
2009	156,001	782	782	—	—	782	—
2010	209,107	1,923	1,774	149	450	1,324	243
2011	181,275	14,450	8,949	5,501	—	8,949	8,865
2012	251,975	16,905	7,367	9,538	—	7,367	37,166
2013	228,158	17,315	7,136	10,179	—	7,136	71,083
2014	149,153	11,758	4,355				