

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2015

OR

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: 001-15749

ALLIANCE DATA SYSTEMS CORPORATION

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

31-1429215

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

7500 Dallas Parkway, Suite 700

Plano, Texas 75024

(Address of principal executive office, including zip code)

(214) 494-3000

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required 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 Regulations S-T (§232.405 of this chapter) 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 definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)

Smaller reporting company

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

As of October 31, 2015, 61,138,307 shares of common stock were outstanding.

INDEX

| | <u>Page Number</u> |
|---|------------------------|
| Part I: FINANCIAL INFORMATION | |
| Item 1. Financial Statements (unaudited) | |
| Condensed Consolidated Balance Sheets as of September 30, 2015 and December 31, 2014 | 3 |
| Condensed Consolidated Statements of Income for the three and nine months ended September 30, 2015 and 2014 | 4 |
| Condensed Consolidated Statements of Comprehensive Income for the three and nine months ended September 30, 2015 and 2014 | 5 |
| Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2015 and 2014 | 6 |
| Notes to Condensed Consolidated Financial Statements | 7 |
| Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations | 34 |
| Item 3. Quantitative and Qualitative Disclosures About Market Risk | 48 |
| Item 4. Controls and Procedures | 48 |
| Part II: OTHER INFORMATION | |
| Item 1. Legal Proceedings | 49 |
| Item 1A. Risk Factors | 49 |
| Item 2. Unregistered Sales of Equity Securities and Use of Proceeds | 52 |
| Item 3. Defaults Upon Senior Securities | 52 |
| Item 4. Mine Safety Disclosures | 52 |
| Item 5. Other Information | 52 |
| Item 6. Exhibits | 53 |
| SIGNATURES | 55 |

PART I

Item 1. Financial Statements.

ALLIANCE DATA SYSTEMS CORPORATION
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

| | September 30, 2015 | December 31, 2014 |
|---|--|----------------------|
| | (In thousands, except per share amounts) | |
| ASSETS | | |
| Cash and cash equivalents | \$ 977,341 | \$ 1,077,152 |
| Trade receivables, less allowance for doubtful accounts (\$3,643 and \$3,811 at September 30, 2015 and December 31, 2014, respectively) | 642,681 | 743,294 |
| Credit card and loan receivables: | | |
| Credit card receivables – restricted for securitization investors | 8,589,282 | 8,312,291 |
| Other credit card and loan receivables | 3,210,737 | 2,931,589 |
| Total credit card and loan receivables | 11,800,019 | 11,243,880 |
| Allowance for loan loss | (671,246) | (570,171) |
| Credit card and loan receivables, net | 11,128,773 | 10,673,709 |
| Credit card and loan receivables held for sale | 98,709 | 125,060 |
| Deferred tax asset, net | 237,723 | 218,872 |
| Other current assets | 544,069 | 456,349 |
| Redemption settlement assets, restricted | 468,417 | 520,340 |
| Total current assets | 14,097,713 | 13,814,776 |
| Property and equipment, net | 561,300 | 559,628 |
| Deferred tax asset, net | 841 | 164 |
| Cash collateral, restricted | 4,888 | 22,511 |
| Intangible assets, net | 1,268,627 | 1,515,994 |
| Goodwill | 3,835,419 | 3,865,484 |
| Other non-current assets | 531,886 | 485,420 |
| Total assets | <u>\$ 20,300,674</u> | <u>\$ 20,263,977</u> |
| LIABILITIES AND EQUITY | | |
| Accounts payable | \$ 382,220 | \$ 455,656 |
| Accrued expenses | 395,467 | 457,472 |
| Contingent consideration | — | 326,023 |
| Deposits | 2,589,313 | 2,645,995 |
| Non-recourse borrowings of consolidated securitization entities | 1,230,000 | 1,058,750 |
| Current debt | 389,146 | 208,164 |
| Other current liabilities | 280,720 | 306,123 |
| Deferred revenue | 703,774 | 846,370 |
| Deferred tax liability, net | 1,719 | 930 |
| Total current liabilities | 5,972,359 | 6,305,483 |
| Deferred revenue | 148,443 | 166,807 |
| Deferred tax liability, net | 642,069 | 690,175 |
| Deposits | 2,633,109 | 2,127,546 |
| Non-recourse borrowings of consolidated securitization entities | 3,743,166 | 4,133,166 |
| Long-term and other debt | 4,710,032 | 4,001,082 |
| Other liabilities | 266,764 | 207,772 |
| Total liabilities | 18,115,942 | 17,632,031 |
| Commitments and contingencies (Note 12) | | |
| Redeemable non-controlling interest | 236,847 | 235,566 |
| Stockholders' equity: | | |
| Common stock, \$0.01 par value; authorized, 200,000 shares; issued, 112,072 shares and 111,686 shares at September 30, 2015 and December 31, 2014, respectively | 1,121 | 1,117 |
| Additional paid-in capital | 2,956,814 | 2,905,563 |
| Treasury stock, at cost, 50,949 shares and 47,874 shares at September 30, 2015 and December 31, 2014, respectively | (3,840,253) | (2,975,795) |
| Retained earnings | 2,948,081 | 2,540,948 |
| Accumulated other comprehensive loss | (117,878) | (75,453) |
| Total stockholders' equity | 1,947,885 | 2,396,380 |
| Total liabilities and equity | <u>\$ 20,300,674</u> | <u>\$ 20,263,977</u> |

See accompanying notes to unaudited condensed consolidated financial statements.

ALLIANCE DATA SYSTEMS CORPORATION
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF INCOME

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|--|-------------------|------------------------------------|-------------------|
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands, except per share amounts) | | | |
| Revenues | | | | |
| Transaction | \$ 83,126 | \$ 87,162 | \$ 263,195 | \$ 251,390 |
| Redemption | 220,922 | 232,464 | 747,192 | 744,658 |
| Finance charges, net | 737,918 | 597,892 | 2,101,360 | 1,672,339 |
| Marketing services | 498,955 | 353,525 | 1,435,520 | 1,021,813 |
| Other revenue | 48,196 | 48,090 | 143,625 | 126,991 |
| Total revenue | <u>1,589,117</u> | <u>1,319,133</u> | <u>4,690,892</u> | <u>3,817,191</u> |
| Operating expenses | | | | |
| Cost of operations (exclusive of depreciation and amortization disclosed separately below) | 901,095 | 767,415 | 2,787,501 | 2,323,210 |
| Provision for loan loss | 171,678 | 114,577 | 461,944 | 281,811 |
| General and administrative | 40,890 | 39,169 | 111,992 | 101,498 |
| Regulatory settlement | 64,563 | — | 64,563 | — |
| Depreciation and other amortization | 36,450 | 28,070 | 104,983 | 79,555 |
| Amortization of purchased intangibles | 86,930 | 48,261 | 262,131 | 145,144 |
| Total operating expenses | <u>1,301,606</u> | <u>997,492</u> | <u>3,793,114</u> | <u>2,931,218</u> |
| Operating income | <u>287,511</u> | <u>321,641</u> | <u>897,778</u> | <u>885,973</u> |
| Interest expense | | | | |
| Securitization funding costs | 23,143 | 22,763 | 71,509 | 67,974 |
| Interest expense on deposits | 13,719 | 9,064 | 37,099 | 25,526 |
| Interest expense on long-term and other debt, net | 45,236 | 29,637 | 132,212 | 98,643 |
| Total interest expense, net | <u>82,098</u> | <u>61,464</u> | <u>240,820</u> | <u>192,143</u> |
| Income before income tax | <u>\$ 205,413</u> | <u>\$ 260,177</u> | <u>\$ 656,958</u> | <u>\$ 693,830</u> |
| Provision for income taxes | 75,031 | 95,229 | 231,705 | 253,946 |
| Net income | <u>\$ 130,382</u> | <u>\$ 164,948</u> | <u>\$ 425,253</u> | <u>\$ 439,884</u> |
| Less: net income attributable to non-controlling interest | 1,952 | 706 | 2,927 | 803 |
| Net income attributable to common stockholders | <u>\$ 128,430</u> | <u>\$ 164,242</u> | <u>\$ 422,326</u> | <u>\$ 439,081</u> |
| Net income attributable to common stockholders per share: | | | | |
| Basic | <u>\$ 2.09</u> | <u>\$ 2.84</u> | <u>\$ 6.55</u> | <u>\$ 7.98</u> |
| Diluted | <u>\$ 2.08</u> | <u>\$ 2.74</u> | <u>\$ 6.51</u> | <u>\$ 6.98</u> |
| Weighted average shares: | | | | |
| Basic | <u>61,430</u> | <u>57,742</u> | <u>62,149</u> | <u>54,998</u> |
| Diluted | <u>61,796</u> | <u>59,908</u> | <u>62,567</u> | <u>62,887</u> |

See accompanying notes to unaudited condensed consolidated financial statements.

ALLIANCE DATA SYSTEMS CORPORATION
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

| | Three Months Ended | | Nine Months Ended | |
|--|---------------------------|-------------|--------------------------|-------------|
| | September 30, | | September 30, | |
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands) | | | |
| Net income | \$ 130,382 | \$ 164,948 | \$ 425,253 | \$ 439,884 |
| Other comprehensive income (loss), net of tax: | | | | |
| Net unrealized gain (loss) on securities available-for-sale, net of tax expense (benefit) of \$700, \$(228), \$572 and \$688 for the three and nine months ended September 30, 2015 and 2014, respectively | 420 | (1,991) | (1,034) | (1,435) |
| Net unrealized gain (loss) on cash flow hedges, net of tax expense (benefit) of \$406, \$(34), \$(510) and \$(34) for the three and nine months ended September 30, 2015 and 2014, respectively | 1,415 | (104) | (1,466) | (104) |
| Foreign currency translation adjustments | 4,633 | (37,956) | (39,925) | (34,480) |
| Other comprehensive income (loss) | 6,468 | (40,051) | (42,425) | (36,019) |
| Total comprehensive income, net of tax | \$ 136,850 | \$ 124,897 | \$ 382,828 | \$ 403,865 |
| Less: comprehensive income attributable to non-controlling interest | 2,363 | 1,251 | 3,360 | 1,514 |
| Comprehensive income attributable to common stockholders | \$ 134,487 | \$ 123,646 | \$ 379,468 | \$ 402,351 |

See accompanying notes to unaudited condensed consolidated financial statements.

ALLIANCE DATA SYSTEMS CORPORATION
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

Nine Months Ended
September 30,

| | |
|-----------------------|-------------|
| 2015 | 2014 |
| (In thousands) | |

CASH FLOWS FROM OPERATING ACTIVITIES:

| | | | | |
|---|----|-------------|----|-------------|
| Net income | \$ | 425,253 | \$ | 439,884 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | | |
| Depreciation and amortization | | 367,114 | | 224,699 |
| Deferred income tax (benefit) expense | | (62,807) | | 5,320 |
| Provision for loan loss | | 461,944 | | 281,811 |
| Non-cash stock compensation | | 73,343 | | 49,754 |
| Amortization of discount on debt | | 646 | | 12,499 |
| Amortization of deferred financing costs | | 23,489 | | 17,092 |
| Change in deferred revenue | | (34,168) | | (41,537) |
| Change in contingent consideration | | (99,601) | | — |
| Change in other operating assets and liabilities, net of acquisitions | | (82,996) | | 21,786 |
| Originations of credit card and loan receivables held for sale | | (4,569,806) | | (3,645,315) |
| Sales of credit card and loan receivables held for sale | | 4,556,339 | | 3,636,809 |
| Excess tax benefits from stock-based compensation | | (22,952) | | (31,888) |
| Other | | (4,566) | | (2,935) |
| Net cash provided by operating activities | | 1,031,232 | | 967,979 |

CASH FLOWS FROM INVESTING ACTIVITIES:

| | | | | |
|---|--|-------------|--|-------------|
| Change in redemption settlement assets | | (16,374) | | (48,906) |
| Change in cash collateral, restricted | | 18,000 | | (1,582) |
| Change in restricted cash | | (369) | | (316,071) |
| Change in credit card and loan receivables | | (913,803) | | (633,336) |
| Purchase of credit card portfolios | | — | | (379,616) |
| Proceeds from the sale of a credit card portfolio | | 26,900 | | — |
| Payment for acquired businesses, net of cash | | (45,430) | | (259,514) |
| Capital expenditures | | (140,091) | | (114,595) |
| Purchases of other investments | | (38,772) | | (109,780) |
| Maturities/sales of other investments | | 7,981 | | 4,565 |
| Other | | (1,011) | | (4,000) |
| Net cash used in investing activities | | (1,102,969) | | (1,862,835) |

CASH FLOWS FROM FINANCING ACTIVITIES:

| | | | | |
|--|--|-------------|--|-------------|
| Borrowings under debt agreements | | 2,426,443 | | 1,920,190 |
| Repayments of borrowings | | (1,528,890) | | (1,580,796) |
| Proceeds from convertible note hedge counterparties | | — | | 1,519,833 |
| Settlement of convertible note borrowings | | — | | (1,864,803) |
| Payment of acquisition-related contingent consideration | | (205,928) | | — |
| Acquisition of non-controlling interest | | (87,376) | | — |
| Issuances of deposits | | 2,191,885 | | 2,342,836 |
| Repayments of deposits | | (1,743,004) | | (1,431,392) |
| Non-recourse borrowings of consolidated securitization entities | | 2,570,000 | | 1,495,000 |
| Repayments/maturities of non-recourse borrowings of consolidated securitization entities | | (2,788,750) | | (1,635,000) |
| Payment of deferred financing costs | | (16,396) | | (24,470) |
| Excess tax benefits from stock-based compensation | | 22,952 | | 31,888 |
| Proceeds from issuance of common stock | | 8,775 | | 10,439 |
| Purchase of treasury shares | | (856,855) | | (217,486) |
| Other | | — | | (1,476) |
| Net cash (used in) provided by financing activities | | (7,144) | | 564,763 |
| Effect of exchange rate changes on cash and cash equivalents | | (20,930) | | (4,905) |
| Change in cash and cash equivalents | | (99,811) | | (334,998) |
| Cash and cash equivalents at beginning of period | | 1,077,152 | | 969,822 |
| Cash and cash equivalents at end of period | | \$ 977,341 | | \$ 634,824 |

SUPPLEMENTAL CASH FLOW INFORMATION:

| | | | | |
|------------------------|----|------------|----|------------|
| Interest paid | \$ | 223,681 | \$ | 153,839 |
| Income taxes paid, net | | \$ 225,913 | | \$ 147,927 |

See accompanying notes to unaudited condensed consolidated financial statements.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The unaudited condensed consolidated financial statements included herein have been prepared by Alliance Data Systems Corporation ("ADSC" or, including its consolidated subsidiaries and variable interest entities ("VIEs"), the "Company"), without audit, pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") have been condensed or omitted pursuant to such rules and regulations. However, the Company believes that the disclosures are adequate to make the information presented not misleading. These unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto included in the Company's Annual Report filed on Form 10-K for the year ended December 31, 2014, filed with the SEC on February 27, 2015.

The unaudited condensed consolidated financial statements included herein reflect all adjustments (consisting of normal, recurring adjustments) which are, in the opinion of management, necessary to state fairly the results for the interim periods presented. The results of operations for the interim periods presented are not necessarily indicative of the operating results to be expected for any subsequent interim period or for the fiscal year.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect (1) the reported amounts of assets; (2) liabilities and disclosure of contingent assets and liabilities at the date of the financial statements; and (3) the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

For purposes of comparability, certain prior period amounts have been reclassified to conform to the current year presentation in accordance with GAAP.

Recently Issued Accounting Standards

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, "Revenue from Contracts with Customers," which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. Companies may adopt ASU 2014-09 using a full retrospective approach or report the cumulative effect as of the date of adoption. On July 9, 2015, the FASB voted to defer the effective date by one year to December 15, 2017 for interim and annual reporting periods beginning after that date and permitted early adoption of the standard, but not before the original effective date of December 15, 2016. The Company is evaluating the impact that adoption of ASU 2014-09 will have on its consolidated financial statements.

In February 2015, the FASB issued ASU 2015-02, "Amendments to the Consolidation Analysis," which amends the consolidation requirements in Accounting Standards Codification ("ASC") 810, "Consolidation." ASU 2015-02 makes targeted amendments to the current consolidation guidance for VIEs, which could change consolidation conclusions. ASU 2015-02 is effective for interim and annual periods beginning after December 15, 2015, with early application permitted. The Company does not expect the adoption of this standard to materially impact its consolidated financial statements.

In April 2015, the FASB issued ASU 2015-03, "Simplifying the Presentation of Debt Issuance Costs." ASU 2015-03 requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. ASU 2015-03 is effective for interim and annual reporting periods beginning after December 15, 2015, with early application permitted. Under ASU 2015-03, unamortized debt issuance costs of \$84.9 million would be reclassified from other non-current assets to a reduction of debt as of September 30, 2015.

In April 2015, the FASB issued ASU 2015-05, "Customer's Accounting for Fees Paid in a Cloud Computing Arrangement." ASU 2015-05 provides guidance about whether a cloud computing arrangement includes a software license and is effective for interim and annual reporting periods beginning after December 15, 2015, with early adoption permitted. The Company does not expect the adoption of this standard to materially impact its consolidated financial statements.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

In July 2015, the FASB issued ASU 2015-11, "Simplifying the Measurement of Inventory." ASU 2015-11 changes the measurement principle for inventory from the lower of cost or market to lower of cost and net realizable value. Net realizable value is defined as the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. ASU 2015-11 is effective for interim and annual reporting periods beginning after December 15, 2016, with early adoption permitted. The Company does not expect the adoption of this standard to materially impact its consolidated financial statements.

2. EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted net income per share for the periods indicated:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|-------------------|--|-------------------|
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands, except per share amounts) | | | |
| Numerator: | | | | |
| Net income attributable to common stockholders | \$ 128,430 | \$ 164,242 | \$ 422,326 | \$ 439,081 |
| Less: accretion of redeemable non-controlling interest | — | — | 15,194 | — |
| Net income attributable to common stockholders after accretion of redeemable non-controlling interest | <u>\$ 128,430</u> | <u>\$ 164,242</u> | <u>\$ 407,132</u> | <u>\$ 439,081</u> |
| Denominator: | | | | |
| Weighted average shares, basic | 61,430 | 57,742 | 62,149 | 54,998 |
| Weighted average effect of dilutive securities: | | | | |
| Shares from assumed conversion of convertible senior notes | — | — | — | 2,816 |
| Shares from assumed exercise of convertible note warrants | — | 1,664 | — | 4,561 |
| Net effect of dilutive stock options and unvested restricted stock | 366 | 502 | 418 | 512 |
| Denominator for diluted calculations | <u>61,796</u> | <u>59,908</u> | <u>62,567</u> | <u>62,887</u> |
| Net income attributable to common stockholders per share: | | | | |
| Basic | <u>\$ 2.09</u> | <u>\$ 2.84</u> | <u>\$ 6.55</u> | <u>\$ 7.98</u> |
| Diluted | <u>\$ 2.08</u> | <u>\$ 2.74</u> | <u>\$ 6.51</u> | <u>\$ 6.98</u> |

3. ACQUISITIONS

2014 Acquisitions:

Brand Loyalty Group B.V.

On January 2, 2014, the Company acquired a 60% ownership interest in BrandLoyalty Group B.V. ("BrandLoyalty"), a Netherlands-based, data-driven loyalty marketer. BrandLoyalty designs, organizes, implements and evaluates innovative and tailor-made loyalty programs for food retailers worldwide. The acquisition expands the Company's presence across Europe, Asia and Latin America. The results of BrandLoyalty have been included since the date of acquisition and are reflected in the Company's LoyaltyOne® segment. The initial cash consideration was approximately \$259.5 million in addition to the assumption of debt. The goodwill resulting from the acquisition is not deductible for tax purposes.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

The following table summarizes the final allocation of consideration and the respective fair values of the assets acquired and liabilities assumed in the BrandLoyalty acquisition as of the date of purchase:

| | As of January 2, 2014 (In thousands) |
|---|---|
| Current assets, net of cash acquired | \$ 246,769 |
| Deferred tax asset | 3,509 |
| Property and equipment | 19,719 |
| Other non-current assets | 3,994 |
| Intangible assets | 423,832 |
| Goodwill | 565,015 |
| Total assets acquired | 1,262,838 |
| Current liabilities | 146,559 |
| Current portion of long-term debt | 34,180 |
| Deferred tax liability | 105,512 |
| Long-term debt (net of current portion) | 126,323 |
| Other liabilities | 142 |
| Total liabilities assumed | 412,716 |
| Redeemable non-controlling interest | 341,907 |
| Net assets acquired | \$ 508,215 |

As part of the initial purchase price allocation, the Company recorded a liability for the earn-out provision included in the BrandLoyalty share purchase agreement of €181.9 million (\$248.7 million as of January 2, 2014). The liability was measured at fair value on the date of purchase and subsequent changes in the fair value of the liability were included in operating expenses in the Company's consolidated statements of income. On February 10, 2015, the Company paid €269.9 million (\$305.5 million) to settle the contingent liability.

Conversant, Inc.

On December 10, 2014, the Company completed the acquisition of 100% of the common stock of Conversant, Inc. ("Conversant"), a digital marketing services company offering unique end-to-end digital marketing solutions that empower clients to more effectively market to their customers across all channels. The results of Conversant® have been included since the date of the acquisition and are reflected in the Company's Epsilon® segment.

The Company paid total consideration of approximately \$2.3 billion, with cash consideration of approximately \$936.3 million, net of cash acquired and equity consideration of approximately \$1.3 billion through the issuance of approximately 4.6 million shares and the exchange of certain restricted stock awards and stock options. The cash and equity consideration paid and issued were determined in accordance with the terms of the merger agreement, with the value based on the volume weighted average price per share of the Company's common stock for the consecutive period of 15 trading days ending on the close of trading on the second trading day immediately preceding the closing of the merger. The goodwill recognized is attributable to expected synergies and an assembled workforce. The goodwill resulting from the acquisition is not deductible for tax purposes.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

In the first quarter of 2015, the Company finalized the purchase price allocation, with no changes from the preliminary purchase price allocation disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2014. The following table summarizes the allocation of the consideration and the respective fair values of the assets acquired and liabilities assumed in the Conversant acquisition as of the date of purchase:

| | As of December 10, 2014 |
|--------------------------------------|------------------------------------|
| | (In thousands) |
| Current assets, net of cash acquired | \$ 180,030 |
| Deferred tax asset | 11,905 |
| Property and equipment | 25,555 |
| Developed technology | 182,500 |
| Other non-current assets | 1,744 |
| Intangible assets | 755,600 |
| Goodwill | 1,650,299 |
| Total assets acquired | 2,807,633 |
| Current liabilities | 177,585 |
| Deferred tax liability | 344,081 |
| Other liabilities | 26,933 |
| Total liabilities assumed | 548,599 |
| Net assets acquired | \$ 2,259,034 |

The following table presents the Company's unaudited pro forma consolidated revenue and net income for the three and nine months ended September 30, 2014. The unaudited pro forma results include the historical consolidated statements of income of the Company and Conversant, giving effect to the Conversant acquisition and related financing transactions as if they had occurred on January 1, 2013.

| | Three Months Ended September 30, 2014 | Nine Months Ended September 30, 2014 |
|--|--|---|
| | (In thousands, except per share amounts) | |
| Total revenue | \$ 1,457,446 | \$ 4,238,797 |
| Net income | \$ 151,921 | \$ 411,476 |
| Net income attributable to common stockholders | \$ 151,215 | \$ 410,673 |
| Net income attributable to common stockholders per share: | | |
| Basic | \$ 2.43 | \$ 6.89 |
| Diluted | \$ 2.34 | \$ 6.08 |

The unaudited pro forma results are not necessarily indicative of the operating results that would have occurred if the Conversant acquisition had been completed as of the date for which the unaudited pro forma financial information is presented. The unaudited pro forma financial information for the three and nine months ended September 30, 2014 includes adjustments that are directly related to the acquisition, factually supportable and expected to have a continuing impact. These adjustments include, but are not limited to, amortization related to fair value adjustments to intangible assets and interest expense on acquisition-related debt. The unaudited pro forma financial information for the three months and nine months ended September 30, 2014 exclude \$6.6 million of acquisition costs consisting primarily of advisory, legal and other professional fees.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

2015 Acquisition:**Edison International Concept & Agencies B.V. and Max Holding B.V.**

On August 31, 2015, BrandLoyalty acquired all of the stock of Edison International Concept & Agencies B.V. ("Edison") and Max Holding B.V. ("Merison"), two Netherlands-based loyalty marketers, for consideration of approximately \$45.4 million, net of \$2.2 million of cash and cash equivalents acquired. The acquisition expands BrandLoyalty's short-term loyalty programs into new markets with new brands. Total net assets acquired were \$61.4 million, including \$6.7 million of intangible assets and \$34.7 million of goodwill, with total liabilities assumed of \$16.0 million. The goodwill resulting from the acquisition is not deductible for tax purposes. The results of Edison and Merison have been included since the date of acquisition and are reflected in the Company's LoyaltyOne segment.

4. CREDIT CARD AND LOAN RECEIVABLES

The Company's credit card and loan receivables are the only portfolio segment or class of financing receivables. Quantitative information about the components of credit card and loan receivables is presented in the table below:

| | September 30, 2015 | December 31, 2014 |
|--|-------------------------------|------------------------------|
| | (In thousands) | |
| Principal receivables | \$ 11,297,882 | \$ 10,762,498 |
| Billed and accrued finance charges | 480,315 | 422,838 |
| Other credit card and loan receivables | 21,822 | 58,544 |
| Total credit card and loan receivables | <u>11,800,019</u> | <u>11,243,880</u> |
| Less credit card receivables – restricted for securitization investors | 8,589,282 | 8,312,291 |
| Other credit card and loan receivables | <u>\$ 3,210,737</u> | <u>\$ 2,931,589</u> |

Allowance for Loan Loss

The Company maintains an allowance for loan loss at a level that is appropriate to absorb probable losses inherent in credit card and loan receivables. The allowance for loan loss covers forecasted uncollectible principal as well as unpaid interest and fees. The allowance for loan loss is evaluated monthly for appropriateness.

In estimating the allowance for principal loan losses, management utilizes a migration analysis of delinquent and current credit card and loan receivables. Migration analysis is a technique used to estimate the likelihood that a credit card or loan receivable will progress through the various stages of delinquency and to charge-off. The allowance is maintained through an adjustment to the provision for loan loss. Charge-offs of principal amounts, net of recoveries are deducted from the allowance. In estimating the allowance for uncollectible unpaid interest and fees, the Company utilizes historical charge-off trends, analyzing actual charge-offs for the prior three months. The allowance is maintained through an adjustment to finance charges, net. In evaluating the allowance for loan loss for both principal and unpaid interest and fees, management also considers factors that may impact loan loss experience, including seasoning, loan volume and amounts, seasonality, payment rates and forecasting uncertainties.

Net charge-offs include the principal amount of losses from credit cardholders unwilling or unable to pay their account balances, as well as bankrupt and deceased credit cardholders, less recoveries and exclude charged-off interest, fees and fraud losses. Charged-off interest and fees reduce finance charges, net while fraud losses are recorded as an expense. Credit card and loan receivables, including unpaid interest and fees, are charged-off at the end of the month during which an account becomes 180 days contractually past due, except in the case of customer bankruptcies or death. Credit card and loan receivables, including unpaid interest and fees, associated with customer bankruptcies or death are charged-off at the end of each month subsequent to 60 days after the receipt of notification of the bankruptcy or death, but in any case, not later than the 180-day contractual time frame.

The Company records the actual charge-offs for unpaid interest and fees as a reduction to finance charges, net. Actual charge-offs for unpaid interest and fees were \$88.9 million and \$70.9 million for the three months ended September 30, 2015 and 2014, respectively, and \$258.2 million and \$212.9 million for the nine months ended September 30, 2015 and 2014, respectively.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

The following table presents the Company's allowance for loan loss for the periods indicated:

| | Three Months Ended | | Nine Months Ended | |
|---|---------------------------|-------------------|--------------------------|-------------------|
| | September 30, | | September 30, | |
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands) | | | |
| Balance at beginning of period | \$ 623,316 | \$ 483,580 | \$ 570,171 | \$ 503,169 |
| Provision for loan loss | 171,678 | 114,577 | 461,944 | 281,811 |
| Change in estimate for uncollectible unpaid interest and fees | — | 1,000 | 4,500 | 1,500 |
| Recoveries | 48,767 | 39,074 | 129,623 | 115,548 |
| Principal charge-offs | (172,515) | (126,877) | (494,992) | (390,674) |
| Balance at end of period | <u>\$ 671,246</u> | <u>\$ 511,354</u> | <u>\$ 671,246</u> | <u>\$ 511,354</u> |

Delinquencies

A credit card account is contractually delinquent if the Company does not receive the minimum payment by the specified due date on the cardholder's statement. It is the Company's policy to continue to accrue interest and fee income on all credit card accounts beyond 90 days, except in limited circumstances, until the credit card account balance and all related interest and other fees are paid or charged-off, typically at 180 days delinquent. When an account becomes delinquent, a message is printed on the credit cardholder's billing statement requesting payment. After an account becomes 30 days past due, a proprietary collection scoring algorithm automatically scores the risk of the account becoming further delinquent. The collection system then recommends a collection strategy for the past due account based on the collection score and account balance and dictates the contact schedule and collections priority for the account. If the Company is unable to make a collection after exhausting all in-house collection efforts, the Company may engage collection agencies and outside attorneys to continue those efforts.

The following table presents the delinquency trends of the Company's credit card and loan receivables portfolio:

| | September 30, | % of | December 31, | % of |
|--|---|--------------|---------------------|--------------|
| | 2015 | Total | 2014 | Total |
| | (In thousands, except percentages) | | | |
| Receivables outstanding – principal | \$ 11,297,882 | 100.0% | \$ 10,762,498 | 100.0% |
| Principal receivables balances contractually delinquent: | | | | |
| 31 to 60 days | 175,018 | 1.5% | 157,760 | 1.4% |
| 61 to 90 days | 113,360 | 1.0 | 93,175 | 0.9 |
| 91 or more days | 225,553 | 2.0 | 182,945 | 1.7 |
| Total | <u>\$ 513,931</u> | <u>4.5%</u> | <u>\$ 433,880</u> | <u>4.0%</u> |

Modified Credit Card Receivables

The Company holds certain credit card receivables for which the terms have been modified. The Company's modified credit card receivables include credit card receivables for which temporary hardship concessions have been granted and credit card receivables in permanent workout programs. These modified credit card receivables include concessions consisting primarily of a reduced minimum payment and an interest rate reduction. The temporary programs' concessions remain in place for a period no longer than twelve months, while the permanent programs remain in place through the payoff of the credit card receivables if the credit cardholder complies with the terms of the program. These concessions do not include the forgiveness of unpaid principal, but may involve the reversal of certain unpaid interest or fee assessments. In the case of the temporary programs, at the end of the concession period, credit card receivable terms revert to standard rates. These arrangements are automatically terminated if the customer fails to make payments in accordance with the terms of the program, at which time their account reverts back to its original terms.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

Credit card receivables for which temporary hardship or permanent concessions have been granted are both considered troubled debt restructurings and are collectively evaluated for impairment. Modified credit card receivables are evaluated at their present value with impairment measured as the difference between the credit card receivables balance and the discounted present value of cash flows expected to be collected. Consistent with the Company's measurement of impairment of modified credit card receivables on a pooled basis, the discount rate used for credit card receivables is the average current annual percentage rate the Company applies to non-impaired credit card receivables, which approximates what would have been applied to the pool of modified credit card receivables prior to impairment. In assessing the appropriate allowance for loan loss, these modified credit card receivables are included in the general pool of credit card receivables with the allowance determined under the contingent loss model of ASC 450-20, "Loss Contingencies." If the Company applied accounting under ASC 310-40, "Troubled Debt Restructurings by Creditors," to the modified credit card receivables in these programs, there would not be a material difference in the allowance for loan loss.

The Company had \$155.5 million and \$134.9 million, respectively, as a recorded investment in impaired credit card receivables with an associated allowance for loan loss of \$39.1 million and \$35.2 million, respectively, as of September 30, 2015 and December 31, 2014. These modified credit card receivables represented less than 2% of the Company's total credit card receivables as of both September 30, 2015 and December 31, 2014.

The average recorded investment in impaired credit card receivables was \$149.2 million and \$114.0 million for the three months ended September 30, 2015 and 2014, respectively, and \$141.5 million and \$114.2 million for the nine months ended September 30, 2015 and 2014, respectively.

Interest income on these modified credit card receivables is accounted for in the same manner as other accruing credit card receivables. Cash collections on these modified credit card receivables are allocated according to the same payment hierarchy methodology applied to credit card receivables that are not in such programs. The Company recognized \$3.8 million and \$3.3 million for the three months ended September 30, 2015 and 2014, respectively, and \$10.7 million and \$9.6 million for the nine months ended September 30, 2015 and 2014, respectively, in interest income associated with modified credit card receivables during the period that such credit card receivables were impaired.

The following tables provide information on credit card receivables that are considered troubled debt restructurings as described above, which entered into a modification program during the specified periods:

| | Three Months Ended September 30, 2015 | | | Nine Months Ended September 30, 2015 | | |
|--|---------------------------------------|--------------------------------------|---------------------------------------|--------------------------------------|--------------------------------------|---------------------------------------|
| | Number of Restructurings | Pre-modification Outstanding Balance | Post-modification Outstanding Balance | Number of Restructurings | Pre-modification Outstanding Balance | Post-modification Outstanding Balance |
| | (Dollars in thousands) | | | | | |
| Troubled debt restructurings – credit card receivables | 44,955 | \$ 48,088 | \$ 48,048 | 120,074 | \$ 129,775 | \$ 129,661 |

| | Three Months Ended September 30, 2014 | | | Nine Months Ended September 30, 2014 | | |
|--|---------------------------------------|--------------------------------------|---------------------------------------|--------------------------------------|--------------------------------------|---------------------------------------|
| | Number of Restructurings | Pre-modification Outstanding Balance | Post-modification Outstanding Balance | Number of Restructurings | Pre-modification Outstanding Balance | Post-modification Outstanding Balance |
| | (Dollars in thousands) | | | | | |
| Troubled debt restructurings – credit card receivables | 36,846 | \$ 37,130 | \$ 37,100 | 102,000 | \$ 101,837 | \$ 101,750 |

The tables below summarize troubled debt restructurings that have defaulted in the specified periods where the default occurred within 12 months of their modification date:

| | Three Months Ended September 30, 2015 | | Nine Months Ended September 30, 2015 | |
|--|---------------------------------------|---------------------|--------------------------------------|---------------------|
| | Number of Restructurings | Outstanding Balance | Number of Restructurings | Outstanding Balance |
| | (Dollars in thousands) | | | |
| Troubled debt restructurings that subsequently defaulted – credit card receivables | 20,212 | \$ 21,436 | 55,940 | \$ 57,995 |

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

| | Three Months Ended September 30, 2014 | | Nine Months Ended September 30, 2014 | |
|--|--|--------------------------------|---|--------------------------------|
| | Number of Restructurings | Outstanding Balance | Number of Restructurings | Outstanding Balance |
| (Dollars in thousands) | | | | |
| Troubled debt restructurings that subsequently defaulted – credit card receivables | 14,047 | \$ 14,037 | 44,545 | \$ 44,009 |

Age of Credit Card and Loan Receivables Accounts

The following tables set forth, as of September 30, 2015 and 2014, the number of active credit card and loan receivables accounts with balances and the related principal balances outstanding, based upon the age of the active credit card and loan receivables accounts from origination:

| September 30, 2015 | | | | |
|---|--|--|--|--|
| Age of Accounts Since Origination | Number of Active Accounts with Balances | Percentage of Active Accounts with Balances | Principal Receivables Outstanding | Percentage of Principal Receivables Outstanding |
| (In thousands, except percentages) | | | | |
| 0-12 Months | 5,881 | 29.8% | \$ 2,994,083 | 26.5% |
| 13-24 Months | 3,014 | 15.3 | 1,783,846 | 15.8 |
| 25-36 Months | 2,085 | 10.6 | 1,266,628 | 11.2 |
| 37-48 Months | 1,509 | 7.6 | 917,319 | 8.1 |
| 49-60 Months | 1,107 | 5.6 | 676,015 | 6.0 |
| Over 60 Months | 6,148 | 31.1 | 3,659,991 | 32.4 |
| Total | 19,744 | 100.0% | \$ 11,297,882 | 100.0% |

| September 30, 2014 | | | | |
|---|--|--|--|--|
| Age of Accounts Since Origination | Number of Active Accounts with Balances | Percentage of Active Accounts with Balances | Principal Receivables Outstanding | Percentage of Principal Receivables Outstanding |
| (In thousands, except percentages) | | | | |
| 0-12 Months | 4,869 | 28.2% | \$ 2,220,148 | 25.1% |
| 13-24 Months | 2,554 | 14.8 | 1,282,695 | 14.5 |
| 25-36 Months | 1,781 | 10.3 | 937,043 | 10.6 |
| 37-48 Months | 1,283 | 7.4 | 701,808 | 7.9 |
| 49-60 Months | 969 | 5.6 | 557,911 | 6.3 |
| Over 60 Months | 5,828 | 33.7 | 3,149,984 | 35.6 |
| Total | 17,284 | 100.0% | \$ 8,849,589 | 100.0% |

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

Credit Quality

The Company uses proprietary scoring models developed specifically for the purpose of monitoring the Company's obligor credit quality. The proprietary scoring models are used as a tool in the underwriting process and for making credit decisions. The proprietary scoring models are based on historical data and require various assumptions about future performance. Information regarding customer performance is factored into these proprietary scoring models to determine the probability of an account becoming 90 or more days past due at any time within the next 12 months. Obligor credit quality is monitored at least monthly during the life of an account. The following table reflects composition of the Company's credit card and loan receivables by obligor credit quality as of September 30, 2015 and 2014:

| Probability of an Account Becoming 90 or More Days Past Due or Becoming Charged-off (within the next 12 months) | September 30, 2015 | | September 30, 2014 | |
|--|--|--|--|--|
| | Total Principal Receivables Outstanding | Percentage of Principal Receivables Outstanding | Total Principal Receivables Outstanding | Percentage of Principal Receivables Outstanding |
| (In thousands, except percentages) | | | | |
| No Score | \$ 176,379 | 1.6% | \$ 180,003 | 2.0% |
| 27.1% and higher | 607,856 | 5.4 | 430,333 | 4.9 |
| 17.1% - 27.0% | 944,270 | 8.3 | 829,208 | 9.4 |
| 12.6% - 17.0% | 1,140,013 | 10.1 | 955,459 | 10.8 |
| 3.7% - 12.5% | 4,413,422 | 39.1 | 3,613,024 | 40.8 |
| 1.9% - 3.6% | 2,405,329 | 21.3 | 1,837,713 | 20.8 |
| Lower than 1.9% | 1,610,613 | 14.2 | 1,003,849 | 11.3 |
| Total | <u>\$ 11,297,882</u> | <u>100.0%</u> | <u>\$ 8,849,589</u> | <u>100.0%</u> |

Transfer of Financial Assets

The Company originates loans under an agreement with one of its clients, and after origination, these loan receivables are sold to the client at par value plus accrued interest. These transfers qualify for sale treatment as they meet the conditions established in ASC 860-10, "Transfers and Servicing." Following the sale, the client owns the loan receivables, bears the risk of loss in the event of loan defaults and is responsible for all servicing functions related to the loan receivables. The loan receivables originated by the Company that have not yet been sold to the client were \$62.2 million and \$48.9 million at September 30, 2015 and December 31, 2014, respectively, and are included in credit card and loan receivables held for sale in the Company's unaudited condensed consolidated balance sheets and carried at the lower of cost or fair value. The carrying value of these loan receivables approximates fair value due to the short duration between the date of origination and sale. Originations and sales of these loan receivables held for sale are reflected as operating activities in the Company's unaudited condensed consolidated statements of cash flows.

Upon the client's purchase of the originated loan receivables, the Company is obligated to purchase a participating interest in a pool of loan receivables that includes the loan receivables originated by the Company. Such interest participates on a pro rata basis in the cash flows of the underlying pool of loan receivables, including principal repayments, finance charges, losses and recoveries. The Company bears the risk of loss related to its participation interest in this pool.

During the nine months ended September 30, 2015 and 2014, the Company purchased \$227.7 million and \$181.8 million, respectively, of loan receivables under these agreements.

The total outstanding balance of these loan receivables was \$193.6 million and \$160.6 million as of September 30, 2015 and December 31, 2014, respectively, and was included in other credit card and loan receivables in the Company's unaudited condensed consolidated balance sheets.

Portfolios Held for Sale

The Company has certain credit card portfolios held for sale, which are carried at the lower of cost or fair value, and were \$36.5 million and \$76.2 million as of September 30, 2015 and December 31, 2014, respectively. In June 2015, the Company sold one credit card portfolio previously classified as held for sale for cash proceeds of \$26.9 million and recognized a de minimis gain.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

Securitized Credit Card Receivables

The Company regularly securitizes its credit card receivables through its credit card securitization trusts, consisting of the World Financial Network Credit Card Master Trust, World Financial Network Credit Card Master Note Trust ("Master Trust I") and World Financial Network Credit Card Master Trust III ("Master Trust III") (collectively, the "WFN Trusts"), and World Financial Capital Credit Card Master Note Trust (the "WFC Trust"). The Company continues to own and service the accounts that generate credit card receivables held by the WFN Trusts and the WFC Trust. In its capacity as a servicer, each of the respective banks earns a fee from the WFN Trusts and the WFC Trust to service and administer the credit card receivables, collect payments and charge-off uncollectible receivables. These fees are eliminated and therefore are not reflected in the Company's unaudited condensed consolidated statements of income for the three and nine months ended September 30, 2015 and 2014.

The WFN Trusts and the WFC Trust are VIEs and the assets of these consolidated VIEs include certain credit card receivables that are restricted to settle the obligations of those entities and are not expected to be available to the Company or its creditors. The liabilities of the consolidated VIEs include non-recourse secured borrowings and other liabilities for which creditors or beneficial interest holders do not have recourse to the general credit of the Company.

The tables below present quantitative information about the components of total securitized credit card receivables, delinquencies and net charge-offs:

| | September 30, 2015 | December 31, 2014 |
|---|-------------------------------|------------------------------|
| | (In thousands) | |
| Total credit card receivables – restricted for securitization investors | \$ 8,589,282 | \$ 8,312,291 |
| Principal amount of credit card receivables – restricted for securitization investors, 90 days or more past due | \$ 172,524 | \$ 145,768 |

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|---|-------------|--|-------------|
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands) | | | |
| Net charge-offs of securitized principal | \$ 94,130 | \$ 75,092 | \$ 290,585 | \$ 240,754 |

5. INVENTORIES

Inventories of \$230.4 million and \$220.5 million at September 30, 2015 and December 31, 2014, respectively, consist of finished goods primarily to be utilized as rewards in the Company's loyalty programs and are included in other current assets in the Company's unaudited condensed consolidated balance sheets.

Inventories are stated at the lower of cost or market and valued primarily on a first-in-first-out basis. The Company records valuation adjustments to its inventories if the cost of inventory exceeds the amount it expects to realize from the ultimate sale or disposal of the inventory. These estimates are based on management's judgment regarding future market conditions and an analysis of historical experience.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

6. OTHER INVESTMENTS

Other investments consist of restricted cash, marketable securities and U.S. Treasury bonds and are included in other current assets and other assets in the Company's unaudited condensed consolidated balance sheets. The principal components of other investments, which are carried at fair value, are as follows:

| | September 30, 2015 | | | | December 31, 2014 | | | |
|-----------------------|--------------------|---------------------|----------------------|-------------------|-------------------|---------------------|----------------------|-------------------|
| | Amortized Cost | Unrealized Gains | Unrealized Losses | Fair Value | Amortized Cost | Unrealized Gains | Unrealized Losses | Fair Value |
| | (In thousands) | | | | | | | |
| Restricted cash | \$ 23,414 | \$ — | \$ — | \$ 23,414 | \$ 22,611 | \$ — | \$ — | \$ 22,611 |
| Marketable securities | 125,672 | 851 | (1,007) | 125,516 | 95,669 | 520 | (1,322) | 94,867 |
| U.S. Treasury bonds | 100,051 | 893 | — | 100,944 | 100,072 | 66 | (33) | 100,105 |
| Total | <u>\$ 249,137</u> | <u>\$ 1,744</u> | <u>\$ (1,007)</u> | <u>\$ 249,874</u> | <u>\$ 218,352</u> | <u>\$ 586</u> | <u>\$ (1,355)</u> | <u>\$ 217,583</u> |

The following tables show the unrealized losses and fair value for those investments that were in an unrealized loss position as of September 30, 2015 and December 31, 2014, aggregated by investment category and the length of time that individual securities have been in a continuous loss position:

| | September 30, 2015 | | | | | |
|-----------------------|---------------------|----------------------|----------------------|----------------------|------------------|----------------------|
| | Less than 12 months | | 12 Months or Greater | | Total | |
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| | (In thousands) | | | | | |
| Marketable securities | \$ 18,913 | \$ (153) | \$ 35,783 | \$ (854) | \$ 54,696 | \$ (1,007) |
| Total | <u>\$ 18,913</u> | <u>\$ (153)</u> | <u>\$ 35,783</u> | <u>\$ (854)</u> | <u>\$ 54,696</u> | <u>\$ (1,007)</u> |

| | December 31, 2014 | | | | | |
|-----------------------|---------------------|----------------------|----------------------|----------------------|-------------------|----------------------|
| | Less than 12 months | | 12 Months or Greater | | Total | |
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| | (In thousands) | | | | | |
| Marketable securities | \$ 8,757 | \$ (27) | \$ 48,961 | \$ (1,295) | \$ 57,718 | \$ (1,322) |
| U.S. Treasury bonds | 75,043 | (33) | — | — | 75,043 | (33) |
| Total | <u>\$ 83,800</u> | <u>\$ (60)</u> | <u>\$ 48,961</u> | <u>\$ (1,295)</u> | <u>\$ 132,761</u> | <u>\$ (1,355)</u> |

The amortized cost and estimated fair value of the marketable securities and U.S. Treasury bonds at September 30, 2015 by contractual maturity are as follows:

| | Amortized Cost | Fair Value |
|--|-------------------|-------------------|
| | | (In thousands) |
| Due in one year or less | \$ 31,638 | \$ 31,672 |
| Due after one year through five years | 75,042 | 75,901 |
| Due after five years through ten years | 15,331 | 15,606 |
| Due after ten years | 103,712 | 103,281 |
| Total | <u>\$ 225,723</u> | <u>\$ 226,460</u> |

Market values were determined for each individual security in the investment portfolio. When evaluating the investments for other-than-temporary impairment, the Company reviews factors such as the length of time and extent to which fair value has been below cost basis, the financial condition of the security's issuer, and the Company's intent to sell the security and whether it is more likely than not that the Company will be required to sell the security before recovery of its amortized cost basis. The Company typically invests in highly-rated securities with low probabilities of default and has the intent and ability to hold the investments until maturity. As of September 30, 2015, the Company does not consider the investments to be other-than-temporarily impaired.

There were no realized gains or losses from the sale of investment securities for the three and nine months ended September 30, 2015 and 2014.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

7. REDEMPTION SETTLEMENT ASSETS

Redemption settlement assets consist of cash and cash equivalents and securities available-for-sale and are designated for settling redemptions by collectors of the AIR MILES® Reward Program in Canada under certain contractual relationships with sponsors of the AIR MILES Reward Program. The principal components of redemption settlement assets, which are carried at fair value, are as follows:

| | September 30, 2015 | | | | December 31, 2014 | | | |
|---------------------------|--------------------|------------------|-------------------|-------------------|-------------------|------------------|-------------------|-------------------|
| | Cost | Unrealized Gains | Unrealized Losses | Fair Value | Cost | Unrealized Gains | Unrealized Losses | Fair Value |
| (In thousands) | | | | | | | | |
| Cash and cash equivalents | \$ 272,649 | \$ — | \$ — | \$ 272,649 | \$ 237,127 | \$ — | \$ — | \$ 237,127 |
| Mutual funds | 26,291 | — | (246) | 26,045 | — | — | — | — |
| Corporate bonds | 168,285 | 1,439 | (1) | 169,723 | 280,053 | 3,160 | — | 283,213 |
| Total | \$ 467,225 | \$ 1,439 | \$ (247) | \$ 468,417 | \$ 517,180 | \$ 3,160 | \$ — | \$ 520,340 |

The following table shows the unrealized losses and fair value for those investments that were in an unrealized loss position as of September 30, 2015, aggregated by investment category and the length of time that individual securities have been in a continuous loss position:

| | September 30, 2015 | | | | | |
|-----------------|---------------------|-------------------|----------------------|-------------------|------------------|-------------------|
| | Less than 12 months | | 12 Months or Greater | | Total | |
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| (In thousands) | | | | | | |
| Mutual funds | \$ 26,045 | \$ (246) | \$ — | \$ — | \$ 26,045 | \$ (246) |
| Corporate bonds | 7,675 | (1) | — | — | 7,675 | (1) |
| Total | \$ 33,720 | \$ (247) | \$ — | \$ — | \$ 33,720 | \$ (247) |

There were no investments that were in an unrealized loss position at December 31, 2014.

The amortized cost and estimated fair value of the securities at September 30, 2015 by contractual maturity are as follows:

| | Amortized Cost | Fair Value |
|---------------------------------------|-------------------|-------------------|
| | (In thousands) | |
| Due in one year or less | \$ 128,927 | \$ 129,252 |
| Due after one year through five years | 65,649 | 66,516 |
| Total | \$ 194,576 | \$ 195,768 |

Market values were determined for each individual security in the investment portfolio. When evaluating the investments for other-than-temporary impairment, the Company reviews factors such as the length of time and extent to which fair value has been below cost basis, the financial condition of the security's issuer, and the Company's intent to sell the security and whether it is more likely than not that the Company will be required to sell the security before recovery of its amortized cost basis. The Company typically invests in highly-rated securities with low probabilities of default and has the intent and ability to hold the investments until maturity. As of September 30, 2015, the Company does not consider the investments to be other-than-temporarily impaired.

There were no realized gains or losses from the sale of investment securities for the three and nine months ended September 30, 2015 and 2014.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

8. INTANGIBLE ASSETS AND GOODWILL
Intangible Assets

Intangible assets consist of the following:

| | September 30, 2015 | | | Amortization Life and Method |
|---|---------------------------|---------------------------------|---------------------|---------------------------------------|
| | Gross Assets | Accumulated Amortization | Net | |
| | (In thousands) | | | |
| Finite Lived Assets | | | | |
| Customer contracts and lists | \$ 1,204,572 | \$ (319,976) | \$ 884,596 | 3-12 years—straight line |
| Premium on purchased credit card portfolios | 249,743 | (110,995) | 138,748 | 3-10 years—straight line, accelerated |
| Customer database | 210,300 | (153,887) | 56,413 | 3-10 years—straight line |
| Collector database | 52,572 | (49,507) | 3,065 | 30 years—15% declining balance |
| Publisher networks | 140,200 | (22,344) | 117,856 | 5-7 years—straight line |
| Tradenames | 85,077 | (40,586) | 44,491 | 2-15 years—straight line |
| Purchased data lists | 11,944 | (6,238) | 5,706 | 1-5 years—straight line, accelerated |
| Favorable lease | 6,891 | (1,597) | 5,294 | 3-10 years—straight line |
| Noncompete agreements | 1,300 | (1,192) | 108 | 3 years—straight line |
| | <u>\$ 1,962,599</u> | <u>\$ (706,322)</u> | <u>\$ 1,256,277</u> | |
| Indefinite Lived Assets | | | | |
| Tradenames | 12,350 | — | 12,350 | Indefinite life |
| Total intangible assets | <u>\$ 1,974,949</u> | <u>\$ (706,322)</u> | <u>\$ 1,268,627</u> | |

| | December 31, 2014 | | | Amortization Life and Method |
|---|--------------------------|---------------------------------|---------------------|---------------------------------------|
| | Gross Assets | Accumulated Amortization | Net | |
| | (In thousands) | | | |
| Finite Lived Assets | | | | |
| Customer contracts and lists | \$ 1,328,056 | \$ (295,263) | \$ 1,032,793 | 4-12 years—straight line |
| Premium on purchased credit card portfolios | 289,173 | (114,923) | 174,250 | 3-10 years—straight line, accelerated |
| Customer database | 210,300 | (126,157) | 84,143 | 3-10 years—straight line |
| Collector database | 60,238 | (56,239) | 3,999 | 30 years—15% declining balance |
| Publisher networks | 140,200 | (1,662) | 138,538 | 5-7 years—straight line |
| Tradenames | 86,934 | (29,408) | 57,526 | 2-15 years—straight line |
| Purchased data lists | 12,335 | (6,497) | 5,838 | 1-5 years—straight line, accelerated |
| Favorable lease | 6,891 | (767) | 6,124 | 3-10 years—straight line |
| Noncompete agreements | 1,300 | (867) | 433 | 3 years—straight line |
| | <u>\$ 2,135,427</u> | <u>\$ (631,783)</u> | <u>\$ 1,503,644</u> | |
| Indefinite Lived Assets | | | | |
| Tradenames | 12,350 | — | 12,350 | Indefinite life |
| Total intangible assets | <u>\$ 2,147,777</u> | <u>\$ (631,783)</u> | <u>\$ 1,515,994</u> | |

The estimated amortization expense related to intangible assets for the next five years and thereafter is as follows:

| | For the Years Ending December 31, |
|---|--|
| | (In thousands) |
| 2015 (excluding the nine months ended September 30, 2015) | \$ 81,064 |
| 2016 | 306,826 |
| 2017 | 267,469 |
| 2018 | 208,967 |
| 2019 | 171,248 |
| 2020 & thereafter | 220,703 |

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

Goodwill

The changes in the carrying amount of goodwill for the nine months ended September 30, 2015 are as follows:

| | <u>LoyaltyOne</u> | <u>Epsilon</u> | <u>Card Services</u> (In thousands) | <u>Corporate/Other</u> | <u>Total</u> |
|---|-------------------|---------------------|--|------------------------|---------------------|
| December 31, 2014 | \$ 713,457 | \$ 2,890,295 | \$ 261,732 | \$ — | \$ 3,865,484 |
| Goodwill acquired during the year | 34,712 | — | — | — | 34,712 |
| Effects of foreign currency translation | (63,923) | (854) | — | — | (64,777) |
| September 30, 2015 | <u>\$ 684,246</u> | <u>\$ 2,889,441</u> | <u>\$ 261,732</u> | <u>\$ —</u> | <u>\$ 3,835,419</u> |

9. DEBT

Debt consists of the following:

| <u>Description</u> | <u>September 30,</u> <u>2015</u> | <u>December 31,</u> <u>2014</u> | <u>Maturity</u> | <u>Interest Rate</u> |
|---|-------------------------------------|------------------------------------|---|----------------------|
| | <u>(Dollars in thousands)</u> | | | |
| <i>Long-term and other debt:</i> | | | | |
| 2013 revolving line of credit | \$ 749,000 | \$ — | July 2018 and December 2019 | (1) |
| 2013 term loans | 2,736,875 | 2,603,125 | Various (2) | (1) |
| BrandLoyalty revolving line of credit | 115,325 | 108,789 | August 2018 | (3) |
| Senior notes due 2017 | 397,978 | 397,332 | December 2017 | 5.250% |
| Senior notes due 2020 | 500,000 | 500,000 | April 2020 | 6.375% |
| Senior notes due 2022 | 600,000 | 600,000 | August 2022 | 5.375% |
| Total long-term and other debt | <u>5,099,178</u> | <u>4,209,246</u> | | |
| Less: current portion | 389,146 | 208,164 | | |
| Long-term portion | <u>\$ 4,710,032</u> | <u>\$ 4,001,082</u> | | |
| <i>Deposits:</i> | | | | |
| Certificates of deposit | \$ 4,017,140 | \$ 3,934,906 | Various – October 2015 – November 2021 | 0.25% to 2.80% |
| Money market deposits | 1,205,282 | 838,635 | On demand | (4) |
| Total deposits | <u>5,222,422</u> | <u>4,773,541</u> | | |
| Less: current portion | 2,589,313 | 2,645,995 | | |
| Long-term portion | <u>\$ 2,633,109</u> | <u>\$ 2,127,546</u> | | |
| <i>Non-recourse borrowings of consolidated securitization entities:</i> | | | | |
| Fixed rate asset-backed term note securities | \$ 3,158,166 | \$ 3,376,916 | Various – May 2016 – August 2020 | 0.91% to 4.55% |
| Floating rate asset-backed term note securities | 810,000 | 450,000 | February 2016 and April 2018 | (5) |
| Conduit asset-backed securities | 1,005,000 | 1,365,000 | Various – May 2016 – May 2017 | (6) |
| Total non-recourse borrowings of consolidated securitization entities | <u>4,973,166</u> | <u>5,191,916</u> | | |
| Less: current portion | 1,230,000 | 1,058,750 | | |
| Long-term portion | <u>\$ 3,743,166</u> | <u>\$ 4,133,166</u> | | |

(1) The interest rate is based upon the London Interbank Offered Rate ("LIBOR") plus an applicable margin. At September 30, 2015, the weighted average interest rate was 2.20% and 2.22% for the 2013 revolving line of credit and 2013 term loans, respectively.

(2) The maturity dates for the 2013 term loans are September 2016, July 2018 and December 2019.

(3) The interest rate is based upon the Euro Interbank Offered Rate plus an applicable margin. At September 30, 2015, the weighted average interest rate was 1.20%.

(4) The interest rates are based on the Federal Funds rate. At September 30, 2015, the interest rates ranged from 0.01% to 0.44%.

(5) The interest rates are based upon LIBOR plus an applicable margin. At September 30, 2015, the interest rates ranged from 0.57% to 0.67%.

(6) The interest rate is based upon LIBOR or the asset-backed commercial paper costs of each individual conduit provider plus an applicable margin. At September 30, 2015, the interest rates ranged from 1.12% to 1.75%.

At September 30, 2015, the Company was in compliance with its debt covenants.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

Long-term and other debt

ADSC, as borrower, and ADS Alliance Data Systems, Inc., ADS Foreign Holdings, Inc., Alliance Data Foreign Holdings, Inc., Epsilon Data Management, LLC, Comenity LLC, Comenity Servicing LLC and Aspen Marketing Services, LLC, as guarantors, are party to a credit agreement that provides for \$2.65 billion in term loans (the "2013 term loans") with certain principal repayments and a \$1.3 billion revolving line of credit (the "2013 revolving line of credit" and together with the 2013 term loans, the "2013 Credit Facility"). Total availability under the 2013 revolving line of credit at September 30, 2015 was \$551.0 million.

On March 3, 2015, Conversant LLC and Commission Junction, Inc. were added as guarantors for the 2013 Credit Facility as well as the Senior Notes due 2017, Senior Notes due 2020 and Senior Notes due 2022.

On September 25, 2015, the Company amended the 2013 Credit Facility and borrowed incremental term loans in the aggregate principal amount of \$200.0 million that mature on September 23, 2016. These term loans bear interest at the same rates and are generally subject to the same terms as the existing term loans under the 2013 Credit Facility.

BrandLoyalty Credit Agreement

BrandLoyalty, in which the Company holds a 70% interest, and certain subsidiaries of BrandLoyalty, as borrower and guarantors, amended its credit agreement in August 2015. The BrandLoyalty credit agreement, as amended, provides for a committed revolving line of credit of €62.5 million and an uncommitted revolving line of credit of €62.5 million, both of which are scheduled to mature on August 25, 2018. As of September 30, 2015, the amount outstanding under the BrandLoyalty credit agreement was €103.2 million (\$115.3 million). The BrandLoyalty credit agreement is secured by the accounts receivable, inventory, fixed assets, bank accounts and shares of BrandLoyalty and certain of its subsidiaries.

All advances under the BrandLoyalty credit agreement are denominated in Euros. The interest rate fluctuates and is equal to EURIBOR, as defined in the BrandLoyalty credit agreement, plus an applicable margin based on BrandLoyalty's senior net leverage ratio. The BrandLoyalty credit agreement contains financial covenants, including a senior net leverage ratio, as well as usual and customary negative covenants and customary events of default.

Non-Recourse Borrowings of Consolidated Securitization Entities*Asset-Backed Term Notes*

In April 2015, Master Trust I issued \$500.0 million of asset-backed term notes, \$140.0 million of which were retained by the Company and eliminated from the Company's unaudited condensed consolidated financial statements. These securities mature in April 2018 and have a variable interest rate equal to LIBOR plus a margin of 0.48%.

In June 2015, \$450.0 million of Series 2010-A asset-backed term notes, \$56.2 million of which were retained by the Company and eliminated from the Company's unaudited condensed consolidated financial statements, matured and were repaid.

In August 2015, Master Trust I issued \$625.0 million of asset-backed term notes, \$150.0 million of which were retained by the Company and eliminated from the Company's unaudited condensed consolidated financial statements. These securities mature in August 2020 and have a fixed interest rate of 2.55%.

In September 2015, \$394.7 million of Series 2014-B asset-backed term notes, \$94.7 million of which were retained by the Company and eliminated from the Company's unaudited condensed consolidated financial statements, matured and were repaid.

In October 2015, Master Trust I issued \$389.6 million of asset-backed term notes, \$89.6 million of which were retained by the Company and eliminated from the Company's unaudited condensed consolidated financial statements. These securities mature in May 2017 and have a fixed interest rate of 1.26%.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

Conduit Facilities

The Company has access to committed undrawn capacity through three conduit facilities to support the funding of its credit card receivables through Master Trust I, Master Trust III and the WFC Trust.

In April 2015, Master Trust I amended its 2009-VFN conduit facility, extending the maturity to March 31, 2017.

In May 2015, Master Trust III renewed its 2009-VFC1 conduit facility, increasing the capacity from \$440.0 million to \$900.0 million and extending the maturity to May 1, 2017.

As of September 30, 2015, total capacity under the conduit facilities was \$2.1 billion, of which \$1.0 billion had been drawn and was included in non-recourse borrowings of consolidated securitization entities in the Company's unaudited condensed consolidated balance sheets.

10. DERIVATIVE INSTRUMENTS

The Company uses derivatives to manage risks associated with certain assets and liabilities arising from the potential adverse impact of fluctuations in interest rates and foreign currency exchange rates.

The Company is a party to certain interest rate derivative instruments that involve the receipt of variable rate amounts from counterparties in exchange for the Company making fixed rate payments over the life of the agreement without the exchange of the underlying notional amount. These interest rate derivative instruments are not designated as hedges. Such instruments are not speculative and are used to manage interest rate risk, but do not meet the specific hedge accounting requirements of ASC 815, "Derivatives and Hedging."

The Company enters into foreign currency derivatives to reduce the volatility of the Company's cash flows resulting from changes in foreign currency exchange rates associated with certain inventory transactions, certain of which are designated as cash flow hedges.

The following tables present the fair values of the derivative instruments included within the Company's unaudited condensed consolidated balance sheets as of September 30, 2015 and December 31, 2014:

| | September 30, 2015 | | | |
|---|---------------------------|-------------------|---|--------------------------------|
| | <u>Notional Amount</u> | <u>Fair Value</u> | <u>Balance Sheet Location</u> (In thousands) | <u>Maturity</u> |
| <i>Designated as hedging instruments:</i> | | | | |
| Foreign currency exchange hedges | \$ 25,208 | \$ 1,454 | Other current assets | October 2015 to September 2016 |
| Foreign currency exchange hedges | \$ 34,675 | \$ 352 | Other current liabilities | October 2015 to May 2016 |
| <i>Not designated as hedging instruments:</i> | | | | |
| Foreign currency exchange hedges | \$ 4,610 | \$ 29 | Other current liabilities | October 2015 |
| Interest rate derivatives | \$ 43,590 | \$ 62 | Other current liabilities | December 2015 |
| December 31, 2014 | | | | |
| | <u>Notional Amount</u> | <u>Fair Value</u> | <u>Balance Sheet Location</u> (In thousands) | <u>Maturity</u> |
| <i>Designated as hedging instruments:</i> | | | | |
| Foreign currency exchange hedges | \$ 50,908 | \$ 3,528 | Other current assets | January 2015 to September 2015 |
| <i>Not designated as hedging instruments:</i> | | | | |
| Foreign currency exchange hedges | \$ 3,125 | \$ 343 | Other current assets | January 2015 to March 2015 |
| Foreign currency exchange forward contract | \$ 236,578 | \$ 16,990 | Other current liabilities | January 2015 |
| Interest rate derivatives | \$ 79,429 | \$ 330 | Other current liabilities | December 2015 to August 2016 |

A gain of \$1.4 million and a loss of \$1.5 million, net of tax, were recognized in other comprehensive income (loss) for the three and nine months ended September 30, 2015, respectively. Changes in the fair value of these hedges, excluding any ineffective portion are recorded in other comprehensive income (loss) until the hedged transactions affect net income. The ineffective portion of these cash flow hedges impacts net income when the ineffectiveness occurs. For the three and nine months ended September 30, 2015, a gain of \$0.7 million and a loss of \$0.3 million, respectively, net of tax, were reclassified from accumulated other comprehensive income into net income and no ineffectiveness was recorded. At September 30, 2015, a de minimis amount of losses is expected to be reclassified from accumulated other comprehensive income into net income in the coming 12 months.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

The following tables summarize activity related to and identify the location of the Company's outstanding derivatives not designated as hedging instruments for the three and nine months ended September 30, 2015 and 2014 recognized in the Company's unaudited condensed consolidated statements of income:

| For the three months ended September 30, | 2015 | | 2014 | |
|---|--|---|--|---|
| | Income Statement Location | Gain (Loss) on Derivative Instruments | Income Statement Location | Gain (Loss) on Derivative Instruments |
| (In thousands) | | | | |
| Interest rate derivatives | Interest expense on long-term and other debt, net | \$ 121 | Interest expense on long-term and other debt, net | \$ 131 |
| Foreign currency exchange forward contract | General and administrative | \$ — | General and administrative | \$ (7,310) |
| Foreign currency exchange hedges | Cost of operations | \$ (46) | Cost of operations | \$ — |

| For the nine months ended September 30, | 2015 | | 2014 | |
|---|--|---|--|---|
| | Income Statement Location | Gain (Loss) on Derivative Instruments | Income Statement Location | Gain (Loss) on Derivative Instruments |
| (In thousands) | | | | |
| Interest rate derivatives | Interest expense on long-term and other debt, net | \$ 213 | Interest expense on long-term and other debt, net | \$ 244 |
| Foreign currency exchange forward contract | General and administrative | \$ (13,724) | General and administrative | \$ (7,310) |
| Foreign currency exchange hedges | Cost of operations | \$ 376 | Cost of operations | \$ — |

Gains and losses on derivatives not designated as hedging instruments are included in other operating activities in the unaudited condensed consolidated statements of cash flows for all periods presented.

The Company limits its exposure on derivatives by entering into contracts with institutions that are established dealers who maintain certain minimum credit criteria established by the Company. At September 30, 2015, the Company does not maintain any derivative instruments subject to master agreements that would require the Company to post collateral or that contain any credit-risk related contingent features.

11. DEFERRED REVENUE

The AIR MILES Reward Program collects fees from its sponsors based on the number of AIR MILES reward miles issued and, in limited circumstances, the number of AIR MILES reward miles redeemed. Because management has determined that the earnings process is not complete at the time an AIR MILES reward mile is issued, the recognition of redemption and service revenue is deferred.

A reconciliation of deferred revenue for the AIR MILES Reward Program is as follows:

| | Deferred Revenue | | |
|--|------------------|------------------------------|--------------|
| | Service | Redemption (In thousands) | Total |
| December 31, 2014 | \$ 332,368 | \$ 680,809 | \$ 1,013,177 |
| Cash proceeds | 146,928 | 278,466 | 425,394 |
| Revenue recognized | (140,018) | (319,382) | (459,400) |
| Other | — | 15 | 15 |
| Effects of foreign currency translation | (42,680) | (84,289) | (126,969) |
| September 30, 2015 | \$ 296,598 | \$ 555,619 | \$ 852,217 |
| Amounts recognized in the unaudited condensed consolidated balance sheets: | | | |
| Current liabilities | \$ 148,155 | \$ 555,619 | \$ 703,774 |
| Non-current liabilities | \$ 148,443 | \$ — | \$ 148,443 |

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

12. COMMITMENTS AND CONTINGENCIES

Litigation and Regulatory Matters

On September 8, 2015, Comenity Bank and Comenity Capital Bank (collectively, the "Banks") each entered into a consent order with the Federal Deposit Insurance Corporation ("FDIC") in settlement of the FDIC's review of the Banks' practices regarding the marketing, promotion and sale of certain add-on products. The Banks entered into the consent orders for the purpose of resolving these matters without admitting or denying any violations of law or regulation set forth in the orders.

Under the consent orders, the Banks will collectively provide restitution of approximately \$61.5 million to eligible customers for actions occurring between January 2008 and September 2014. In addition, the Banks collectively agreed to pay \$2.5 million in civil money penalties to the FDIC. Adequate provisions have been made for these costs in the Company's consolidated financial statements as of September 30, 2015. Before the FDIC's review began, the Banks made changes to these add-on products, and they believe their current business practices substantially address the FDIC's concerns; however, the Banks also agreed to make further enhancements to their compliance and other processes related to the marketing, promotion and sale of these add-on products.

13. REDEEMABLE NON-CONTROLLING INTEREST

On January 2, 2014, the Company acquired a 60% ownership interest in BrandLoyalty. Pursuant to the BrandLoyalty share purchase agreement, the Company may acquire the remaining 40% ownership interest in BrandLoyalty over a four-year period from the acquisition date at 10% per year at predetermined valuation multiples. If specified annual earnings targets are met by BrandLoyalty, the Company must acquire the additional 10% ownership interest for the year achieved; otherwise, the sellers have a put option to sell the Company their 10% ownership interest for the respective year.

The specified annual earnings target was met for the year ended December 31, 2014 and the Company acquired an additional 10% ownership interest effective January 1, 2015, increasing its ownership percentage to 70%. The Company paid €77.2 million on February 10, 2015 (\$87.4 million) to acquire this additional 10% ownership interest. The remaining 30% interests held by minority interest shareholders are considered redeemable non-controlling interests, as the acquisition of these interests is outside of the Company's control.

As of September 30, 2015, the remaining interests are not redeemable, but are probable to be redeemed. As such, the Company adjusted the carrying amount of the redeemable non-controlling interest to the estimated redemption value assuming the interests were redeemable as of September 30, 2015. The estimated redemption values are based on a formula as prescribed in the BrandLoyalty share purchase agreement.

A reconciliation of the changes in the redeemable non-controlling interest is as follows:

| | Redeemable Non-Controlling Interest |
|---|--|
| | (In thousands) |
| Balance at January 2, 2014 | \$ 341,907 |
| Net income attributable to non-controlling interest | 9,847 |
| Other comprehensive income attributable to non-controlling interest | 1,988 |
| Adjustment to redemption value | 14,775 |
| Foreign currency translation adjustments | (39,654) |
| Reclassification to accrued expenses | (93,297) |
| Balance at December 31, 2014 | 235,566 |
| Net income attributable to non-controlling interest | 2,927 |
| Other comprehensive income attributable to non-controlling interest | 433 |
| Adjustment to redemption value | 15,194 |
| Foreign currency translation adjustments | (17,273) |
| Balance at September 30, 2015 | \$ 236,847 |

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

14. STOCKHOLDERS' EQUITY

Stock Repurchase Program

On January 1, 2015, the Company's Board of Directors authorized a stock repurchase program to acquire up to \$600.0 million of the Company's outstanding common stock from January 1, 2015 through December 31, 2015. On April 15, 2015, the Company's Board of Directors authorized an increase to the stock repurchase program originally approved on January 1, 2015 to acquire an additional \$400.0 million of the Company's outstanding common stock through December 31, 2015, for a total authorization of \$1.0 billion. The stock repurchase program is subject to any restrictions pursuant to the terms of the Company's credit agreements, indentures, applicable securities laws or otherwise.

For the nine months ended September 30, 2015, the Company acquired a total of 3.1 million shares of its common stock for \$864.5 million, of which \$7.6 million had not settled as of September 30, 2015. As of September 30, 2015, the Company had \$135.5 million available under the stock repurchase program.

Stock Compensation Expense

Total stock-based compensation expense recognized in the Company's unaudited condensed consolidated statements of income for the three and nine months ended September 30, 2015 and 2014 is as follows:

| | Three Months Ended | | Nine Months Ended | |
|----------------------------|---------------------------|------------------|--------------------------|------------------|
| | September 30, | | September 30, | |
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands) | | | |
| Cost of operations | \$ 16,801 | \$ 11,589 | \$ 56,639 | \$ 33,801 |
| General and administrative | 5,012 | 6,668 | 16,704 | 15,953 |
| Total | \$ 21,813 | \$ 18,257 | \$ 73,343 | \$ 49,754 |

During the nine months ended September 30, 2015, the Company awarded 222,605 performance-based restricted stock units with a weighted average grant date fair value per share of \$284.23 as determined on the date of grant. The performance restriction on the awards will lapse upon determination by the Board of Directors or the Compensation Committee of the Board of Directors that the Company's earnings before taxes for the period from January 1, 2015 to December 31, 2015 met certain pre-defined vesting criteria that permit a range from 50% to 150% of such performance-based restricted stock units to vest. Upon such determination, the restrictions will lapse with respect to 33% of the award on February 17, 2016, an additional 33% of the award on February 17, 2017 and the final 34% of the award on February 17, 2018, provided that the participant is employed by the Company on each such vesting date.

During the nine months ended September 30, 2015, the Company awarded 77,798 service-based restricted stock units with a weighted average grant date fair value per share of \$284.77 as determined on the date of grant. Service-based restricted stock units typically vest ratably over three years provided that the participant is employed by the Company on each such vesting date.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

15. ACCUMULATED OTHER COMPREHENSIVE INCOME

The changes in each component of accumulated other comprehensive income (loss), net of tax effects, are as follows:

| Three Months Ended September 30, 2015 | Net Unrealized Gains (Losses) on Securities | Unrealized Gains (Losses) on Cash Flow Hedges | Foreign Currency Translation Adjustments ⁽¹⁾ | Accumulated Other Comprehensive Income (Loss) |
|---|--|--|--|--|
| (In thousands) | | | | |
| Balance at June 30, 2015 | \$ 1,200 | \$ (531) | \$ (125,015) | \$ (124,346) |
| Changes in other comprehensive income (loss) before reclassifications | 420 | 2,073 | 4,633 | 7,126 |
| Amounts reclassified from other comprehensive income (loss) | — | (658) | — | (658) |
| Changes in other comprehensive income (loss) | 420 | 1,415 | 4,633 | 6,468 |
| Balance as of September 30, 2015 | \$ 1,620 | \$ 884 | \$ (120,382) | \$ (117,878) |

| Three Months Ended September 30, 2014 | Net Unrealized Gains (Losses) on Securities | Unrealized Gains (Losses) on Cash Flow Hedges | Foreign Currency Translation Adjustments ⁽¹⁾ | Accumulated Other Comprehensive Income (Loss) |
|--|--|--|--|--|
| (In thousands) | | | | |
| Balance as of June 30, 2014 | \$ 4,745 | \$ — | \$ (18,940) | \$ (14,195) |
| Changes in other comprehensive income (loss) | (1,991) | (104) | (37,956) | (40,051) |
| Balance as of September 30, 2014 | \$ 2,754 | \$ (104) | \$ (56,896) | \$ (54,246) |

| Nine Months Ended September 30, 2015 | Net Unrealized Gains (Losses) on Securities | Unrealized Gains (Losses) on Cash Flow Hedges | Foreign Currency Translation Adjustments ⁽¹⁾ | Accumulated Other Comprehensive Income (Loss) |
|---|--|--|--|--|
| (In thousands) | | | | |
| Balance at December 31, 2014 | \$ 2,654 | \$ 2,350 | \$ (80,457) | \$ (75,453) |
| Changes in other comprehensive income (loss) before reclassifications | (1,034) | (1,813) | (39,925) | (42,772) |
| Amounts reclassified from other comprehensive income (loss) | — | 347 | — | 347 |
| Changes in other comprehensive income (loss) | (1,034) | (1,466) | (39,925) | (42,425) |
| Balance as of September 30, 2015 | \$ 1,620 | \$ 884 | \$ (120,382) | \$ (117,878) |

| Nine Months Ended September 30, 2014 | Net Unrealized Gains (Losses) on Securities | Unrealized Gains (Losses) on Cash Flow Hedges | Foreign Currency Translation Adjustments ⁽¹⁾ | Accumulated Other Comprehensive Income (Loss) |
|--|--|--|--|--|
| (In thousands) | | | | |
| Balance as of December 31, 2013 | \$ 4,189 | \$ — | \$ (22,416) | \$ (18,227) |
| Changes in other comprehensive income (loss) | (1,435) | (104) | (34,480) | (36,019) |
| Balance as of September 30, 2014 | \$ 2,754 | \$ (104) | \$ (56,896) | \$ (54,246) |

⁽¹⁾ Primarily related to the impact of changes in the Canadian dollar and Euro foreign currency exchange rates.

There were no reclassifications out of accumulated other comprehensive income (loss) into net income for the three and nine months ended September 30, 2014.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

16. FINANCIAL INSTRUMENTS

In accordance with ASC 825, "Financial Instruments," the Company is required to disclose the fair value of financial instruments for which it is practical to estimate fair value. To obtain fair values, observable market prices are used if available. In some instances, observable market prices are not readily available and fair value is determined using present value or other techniques appropriate for a particular financial instrument. These techniques involve judgment and as a result are not necessarily indicative of the amounts the Company would realize in a current market exchange. The use of different assumptions or estimation techniques may have a material effect on the estimated fair value amounts.

Fair Value of Financial Instruments — The estimated fair values of the Company's financial instruments as of the specified date are as follows:

| | September 30, 2015 | | December 31, 2014 | |
|---|--------------------|------------|-------------------|--------------|
| | Carrying Amount | Fair Value | Carrying Amount | Fair Value |
| | (In thousands) | | | |
| Financial assets | | | | |
| Cash and cash equivalents | \$ 977,341 | \$ 977,341 | \$ 1,077,152 | \$ 1,077,152 |
| Trade receivables, net | 642,681 | 642,681 | 743,294 | 743,294 |
| Credit card and loan receivables, net | 11,128,773 | 11,128,773 | 10,673,709 | 10,673,709 |
| Credit card and loan receivables held for sale | 98,709 | 98,709 | 125,060 | 125,060 |
| Redemption settlement assets, restricted | 468,417 | 468,417 | 520,340 | 520,340 |
| Cash collateral, restricted | 4,888 | 4,888 | 22,511 | 22,511 |
| Derivative instruments | 1,454 | 1,454 | 3,871 | 3,871 |
| Other investments | 249,874 | 249,874 | 217,583 | 217,583 |
| Financial liabilities | | | | |
| Accounts payable | 382,220 | 382,220 | 455,656 | 455,656 |
| Derivative instruments | 443 | 443 | 17,290 | 17,290 |
| Deposits | 5,222,422 | 5,269,310 | 4,773,541 | 4,801,464 |
| Non-recourse borrowings of consolidated securitization entities | 4,973,166 | 5,018,393 | 5,191,916 | 5,225,359 |
| Long-term and other debt | 5,099,178 | 5,110,950 | 4,209,246 | 4,227,414 |
| Contingent consideration | — | — | 326,023 | 326,023 |

Fair Value of Assets and Liabilities Held at September 30, 2015 and December 31, 2014

The following techniques and assumptions were used by the Company in estimating fair values of financial instruments as disclosed herein:

Cash and cash equivalents, trade receivables, net and accounts payable — The carrying amount approximates fair value due to the short maturity and the relatively liquid nature of these assets and liabilities.

Credit card and loan receivables, net — The carrying amount of credit card and loan receivables, net approximates fair value due to the short maturity and average interest rates that approximate current market origination rates.

Credit card and loan receivables held for sale — Credit card and loan receivables held for sale are recorded at the lower of cost or fair value, and their carrying amount approximates fair value due to the short duration of the holding period of the receivables prior to sale.

Redemption settlement assets, restricted — Redemption settlement assets, restricted are recorded at fair value based on quoted market prices for the same or similar securities.

Cash collateral, restricted — Spread deposits are recorded at their fair value based on discounted cash flow models. The Company uses a valuation model that calculates the present value of estimated cash flows for each asset. The fair value is based on the term of the underlying securities and a discount rate. The carrying amount of excess funding deposits approximates its fair value due to the relatively short maturity period and average interest rates, which approximate current market rates.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

Other investments — Other investments are recorded at fair value based on quoted market prices for the same or similar securities.

Deposits — The fair value is estimated based on the current observable market rates available to the Company for similar deposits with similar remaining maturities.

Non-recourse borrowings of consolidated securitization entities — The fair value is estimated based on the current observable market rates available to the Company for similar debt instruments with similar remaining maturities or quoted market prices for the same transaction.

Long-term and other debt — The fair value is estimated based on the current observable market rates available to the Company for similar debt instruments with similar remaining maturities or quoted market prices for the same transaction.

Derivative instruments — Derivative instruments are recorded at fair value based on a discounted cash flow analysis on the expected cash flows of each derivative. This analysis reflected the contractual terms of the derivatives, including the period to maturity, and used observable market-based inputs, including interest rate curves and option volatility. The fair value of the foreign currency derivative instruments is estimated based on published quotations of spot foreign currency rates and forward points which are converted into implied foreign currency rates.

Contingent consideration — The contingent consideration was recorded at fair value. The fair value at inception was determined using a Monte Carlo simulation valuation technique, which is based on certain key assumptions, including the estimated 2014 earnings and net debt of BrandLoyalty, each as defined in the BrandLoyalty share purchase agreement, earnings volatility, and discount rate. As of December 31, 2014, the fair value was determined based on the provisions in the BrandLoyalty share purchase agreement, which included a defined multiple, 2014 BrandLoyalty EBITDA and net debt. This liability was settled in the first quarter of 2015.

Financial Assets and Financial Liabilities Fair Value Hierarchy

ASC 820 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include:

- Level 1, defined as observable inputs such as quoted prices in active markets;
- Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and
- Level 3, defined as unobservable inputs where little or no market data exists, therefore requiring an entity to develop its own assumptions.

Financial instruments are considered Level 3 when their values are determined using pricing models, discounted cash flow methodologies or similar techniques and at least one significant model assumption or input is unobservable. Level 3 financial instruments also include those for which the determination of fair value requires significant management judgment or estimation. The use of different techniques to determine fair value of these financial instruments could result in different estimates of fair value at the reporting date.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

The following tables provide information for the assets and liabilities carried at fair value measured on a recurring basis as of September 30, 2015 and December 31, 2014:

| | Balance at September 30, 2015 | Fair Value Measurements at September 30, 2015 Using | | |
|---|--|--|-------------------|-----------------|
| | | Level 1 | Level 2 | Level 3 |
| | | (In thousands) | | |
| Corporate bonds ⁽¹⁾ | \$ 169,723 | \$ — | \$ 169,723 | \$ — |
| Mutual funds ⁽¹⁾ | 26,045 | 26,045 | — | — |
| Cash collateral, restricted | 4,888 | — | — | 4,888 |
| Other investments ⁽²⁾ | 249,874 | 129,443 | 120,431 | — |
| Derivative instruments ⁽³⁾ | 1,454 | — | 1,454 | — |
| Total assets measured at fair value | \$ 451,984 | \$ 155,488 | \$ 291,608 | \$ 4,888 |
| Derivative instruments ⁽³⁾ | \$ 443 | \$ — | \$ 443 | \$ — |
| Total liabilities measured at fair value | \$ 443 | \$ — | \$ 443 | \$ — |

| | Balance at December 31, 2014 | Fair Value Measurements at December 31, 2014 Using | | |
|---|---|---|-------------------|-------------------|
| | | Level 1 | Level 2 | Level 3 |
| | | (In thousands) | | |
| Corporate bonds ⁽¹⁾ | \$ 283,213 | \$ — | \$ 283,213 | \$ — |
| Cash collateral, restricted | 22,511 | — | — | 22,511 |
| Other investments ⁽²⁾ | 217,583 | 127,764 | 89,819 | — |
| Derivative instruments ⁽³⁾ | 3,871 | — | 3,871 | — |
| Total assets measured at fair value | \$ 527,178 | \$ 127,764 | \$ 376,903 | \$ 22,511 |
| Derivative instruments ⁽³⁾ | \$ 17,290 | \$ — | \$ 17,290 | \$ — |
| Contingent consideration | 326,023 | — | — | 326,023 |
| Total liabilities measured at fair value | \$ 343,313 | \$ — | \$ 17,290 | \$ 326,023 |

(1) Amounts are included in redemption settlement assets in the unaudited condensed consolidated balance sheets.

(2) Amounts are included in other current assets and other assets in the unaudited condensed consolidated balance sheets.

(3) Derivative instruments are included in other current assets and other current liabilities in the unaudited condensed consolidated balance sheets.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

The following tables summarize the changes in fair values of the Company's asset and liability measured at fair value on a recurring basis using significant unobservable inputs (Level 3) as defined in ASC 825:

Spread deposits included in cash collateral, restricted are recorded at their fair value based on discounted cash flow models, utilizing the term of 13 months. The unobservable input used to calculate the fair value was the discount rate of 3.3%, which was based on an interest rate curve that is observable in the market as adjusted for a credit spread. Significant increases in the term or the discount rate would result in a lower fair value. Conversely, significant decreases in the term or the discount rate would result in a higher fair value.

| | Cash Collateral, Restricted | | | |
|---------------------------------------|------------------------------------|------------------|--------------------------|------------------|
| | Three Months Ended | | Nine Months Ended | |
| | September 30, | | September 30, | |
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands) | | | |
| Balance at beginning of period | \$ 4,841 | \$ 34,710 | \$ 22,511 | \$ 34,124 |
| Total gains (realized or unrealized): | | | | |
| Included in earnings | 47 | 284 | 377 | 870 |
| Purchases | — | — | — | — |
| Sales | — | — | — | — |
| Issuances | — | — | — | — |
| Settlements | — | — | (18,000) | — |
| Transfers in or out of Level 3 | — | — | — | — |
| Balance at end of period | <u>\$ 4,888</u> | <u>\$ 34,994</u> | <u>\$ 4,888</u> | <u>\$ 34,994</u> |

| | | | | |
|---|--------------|---------------|---------------|---------------|
| Gains for the period included in earnings related to assets still held at end of period | <u>\$ 47</u> | <u>\$ 284</u> | <u>\$ 102</u> | <u>\$ 870</u> |
|---|--------------|---------------|---------------|---------------|

For the three and nine months ended September 30, 2015 and 2014, gains included in earnings attributable to cash collateral, restricted are included in securitization funding costs in the Company's unaudited condensed consolidated statements of income.

The contingent consideration represents the additional consideration that the Company was required to pay as part of the earn-out provisions included in the BrandLoyalty share purchase agreement. The fair value was determined based on BrandLoyalty's earnings for the year ended December 31, 2014 using the methodology defined in the BrandLoyalty share purchase agreement. The obligation was settled in the first quarter of 2015.

| | Contingent Consideration | | | |
|---|---------------------------------|-------------------|--------------------------|-------------------|
| | Three Months Ended | | Nine Months Ended | |
| | September 30, | | September 30, | |
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands) | | | |
| Balance at beginning of period | \$ — | \$ 249,067 | \$ 326,023 | \$ — |
| Total gains or losses (realized or unrealized): | | | | |
| Included in earnings | — | — | — | — |
| Purchases | — | — | 547 | 248,702 |
| Sales | — | — | — | — |
| Issuances | — | — | — | — |
| Settlements | — | — | (305,528) | — |
| Foreign currency transaction adjustments | — | (19,286) | (21,042) | (18,921) |
| Transfers in or out of Level 3 | — | — | — | — |
| Balance at end of period | <u>\$ —</u> | <u>\$ 229,781</u> | <u>\$ —</u> | <u>\$ 229,781</u> |
| Gains (losses) for the period included in earnings related to liability still held at end of period | <u>\$ —</u> | <u>\$ 19,286</u> | <u>\$ —</u> | <u>\$ 18,921</u> |

There were no transfers between Level 1 and 2 within the fair value hierarchy for the three and nine months ended September 30, 2015 and 2014.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

Financial Instruments Disclosed but Not Carried at Fair Value

The following tables provide assets and liabilities disclosed but not carried at fair value as of September 30, 2015 and December 31, 2014:

| | Fair Value Measurements at September 30, 2015 | | | |
|---|--|-------------------|----------------------|----------------------|
| | Total | Level 1 | Level 2 | Level 3 |
| | (In thousands) | | | |
| Financial assets | | | | |
| Cash and cash equivalents | \$ 977,341 | \$ 977,341 | \$ — | \$ — |
| Credit card and loan receivables, net | 11,128,773 | — | — | 11,128,773 |
| Credit card and loan receivables held for sale | 98,709 | — | — | 98,709 |
| Total | \$ 12,204,823 | \$ 977,341 | \$ — | \$ 11,227,482 |
| Financial liabilities | | | | |
| Deposits | \$ 5,269,310 | \$ — | \$ 5,269,310 | \$ — |
| Non-recourse borrowings of consolidated securitization entities | 5,018,393 | — | 5,018,393 | — |
| Long-term and other debt | 5,110,950 | — | 5,110,950 | — |
| Total | \$ 15,398,653 | \$ — | \$ 15,398,653 | \$ — |

| | Fair Value Measurements at December 31, 2014 | | | |
|---|---|---------------------|----------------------|----------------------|
| | Total | Level 1 | Level 2 | Level 3 |
| | (In thousands) | | | |
| Financial assets | | | | |
| Cash and cash equivalents | \$ 1,077,152 | \$ 1,077,152 | \$ — | \$ — |
| Credit card and loan receivables, net | 10,673,709 | — | — | 10,673,709 |
| Credit card and loan receivables held for sale | 125,060 | — | — | 125,060 |
| Total | \$ 11,875,921 | \$ 1,077,152 | \$ — | \$ 10,798,769 |
| Financial liabilities | | | | |
| Deposits | \$ 4,801,464 | \$ — | \$ 4,801,464 | \$ — |
| Non-recourse borrowings of consolidated securitization entities | 5,225,359 | — | 5,225,359 | — |
| Long-term and other debt | 4,227,414 | — | 4,227,414 | — |
| Total | \$ 14,254,237 | \$ — | \$ 14,254,237 | \$ — |

17. INCOME TAXES

For the three and nine months ended September 30, 2015, the Company utilized an effective tax rate of 36.5% and 35.3%, respectively, to calculate its provision for income taxes. For each of the three and nine months ended September 30, 2014, the Company utilized an effective tax rate of 36.6%. The effective tax rate for nine months ended September 30, 2015 reflects a favorable state ruling and a lapse in an applicable statute of limitations. In accordance with ASC 740-270, "Income Taxes — Interim Reporting," the Company's expected annual effective tax rate for calendar year 2015 based on all known variables is approximately 35.7%.

18. SEGMENT INFORMATION

Operating segments are defined by ASC 280, "Segment Reporting," as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. The Company's chief operating decision maker is the President and Chief Executive Officer. The operating segments are reviewed separately because each operating segment represents a strategic business unit that generally offers different products.

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

The Company operates in the following reportable segments: LoyaltyOne, Epsilon, and Card Services. In the first quarter of 2015, the Company renamed the Private Label Services and Credit segment to "Card Services," which had no impact to the reported results of the segment in the current or prior periods. Segment operations consist of the following:

- LoyaltyOne includes the Company's Canadian AIR MILES Reward Program and BrandLoyalty;
- Epsilon provides end-to-end, integrated direct marketing solutions that leverage transactional data to help clients more effectively acquire and build stronger relationships with their customers; and
- Card Services provides risk management solutions, account origination, funding, transaction processing, customer care, collections and marketing services for the Company's private label and co-brand credit card programs.

Corporate and other immaterial businesses are reported collectively as an "all other" category labeled "Corporate/Other." Income taxes are not allocated to the segments in the computation of segment operating profit for internal evaluation purposes and have also been included in "Corporate/Other."

| Three Months Ended September 30, 2015 | LoyaltyOne | Epsilon | Card Services | Corporate/ Other | Eliminations | Total |
|--|-----------------------|-------------------|----------------------|-----------------------------|---------------------|-------------------|
| | (In thousands) | | | | | |
| Revenues | \$ 299,143 | \$ 532,448 | \$ 763,997 | \$ 138 | \$ (6,609) | \$ 1,589,117 |
| Income (loss) before income taxes | 47,786 | 42,678 | 202,717 | (87,768) | — | 205,413 |
| Interest expense, net | 709 | 1 | 36,862 | 44,526 | — | 82,098 |
| Operating income (loss) | 48,495 | 42,679 | 239,579 | (43,242) | — | 287,511 |
| Depreciation and amortization | 21,115 | 81,686 | 18,087 | 2,492 | — | 123,380 |
| Stock compensation expense | 2,336 | 10,670 | 3,796 | 5,011 | — | 21,813 |
| Regulatory settlement | — | — | 64,563 | — | — | 64,563 |
| Adjusted EBITDA ⁽¹⁾ | 71,946 | 135,035 | 326,025 | (35,739) | — | 497,267 |
| Less: securitization funding costs | — | — | 23,143 | — | — | 23,143 |
| Less: interest expense on deposits | — | — | 13,719 | — | — | 13,719 |
| Less: adjusted EBITDA attributable to non-controlling interest | 7,455 | — | — | — | — | 7,455 |
| Adjusted EBITDA, net ⁽¹⁾ | <u>\$ 64,491</u> | <u>\$ 135,035</u> | <u>\$ 289,163</u> | <u>\$ (35,739)</u> | <u>\$ —</u> | <u>\$ 452,950</u> |

| Three Months Ended September 30, 2014 | LoyaltyOne | Epsilon | Card Services | Corporate/ Other | Eliminations | Total |
|--|-----------------------|------------------|----------------------|-----------------------------|---------------------|-------------------|
| | (In thousands) | | | | | |
| Revenues | \$ 324,484 | \$ 377,554 | \$ 622,330 | \$ 144 | \$ (5,379) | \$ 1,319,133 |
| Income (loss) before income taxes | 51,078 | 42,597 | 237,053 | (70,551) | — | 260,177 |
| Interest expense, net | 1,303 | (3) | 30,675 | 29,489 | — | 61,464 |
| Operating income (loss) | 52,381 | 42,594 | 267,728 | (41,062) | — | 321,641 |
| Depreciation and amortization | 22,529 | 36,564 | 15,202 | 2,036 | — | 76,331 |
| Stock compensation expense | 2,954 | 5,137 | 3,498 | 6,668 | — | 18,257 |
| Adjusted EBITDA ⁽¹⁾ | 77,864 | 84,295 | 286,428 | (32,358) | — | 416,229 |
| Less: securitization funding costs | — | — | 22,763 | — | — | 22,763 |
| Less: interest expense on deposits | — | — | 9,064 | — | — | 9,064 |
| Less: adjusted EBITDA attributable to non-controlling interest | 8,378 | — | — | — | — | 8,378 |
| Adjusted EBITDA, net ⁽¹⁾ | <u>\$ 69,486</u> | <u>\$ 84,295</u> | <u>\$ 254,601</u> | <u>\$ (32,358)</u> | <u>\$ —</u> | <u>\$ 376,024</u> |

ALLIANCE DATA SYSTEMS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

| Nine Months Ended September 30, 2015 | LoyaltyOne | Epsilon | Card Services | Corporate/ Other | Eliminations | Total |
|--|-------------------|----------------|----------------------|-----------------------------|---------------------|--------------|
| (In thousands) | | | | | | |
| Revenues | \$ 988,755 | \$ 1,532,521 | \$ 2,189,113 | \$ 280 | \$ (19,777) | \$ 4,690,892 |
| Income (loss) before income taxes | 143,919 | 69,496 | 692,423 | (248,880) | — | 656,958 |
| Interest expense, net | 1,994 | (15) | 108,608 | 130,233 | — | 240,820 |
| Operating income (loss) | 145,913 | 69,481 | 801,031 | (118,647) | — | 897,778 |
| Depreciation and amortization | 61,586 | 244,535 | 54,057 | 6,936 | — | 367,114 |
| Stock compensation expense | 8,122 | 37,209 | 11,308 | 16,704 | — | 73,343 |
| Regulatory settlement | — | — | 64,563 | — | — | 64,563 |
| Adjusted EBITDA ⁽¹⁾ | 215,621 | 351,225 | 930,959 | (95,007) | — | 1,402,798 |
| Less: securitization funding costs | — | — | 71,509 | — | — | 71,509 |
| Less: interest expense on deposits | — | — | 37,099 | — | — | 37,099 |
| Less: adjusted EBITDA attributable to non-controlling interest | 18,400 | — | — | — | — | 18,400 |
| Adjusted EBITDA, net ⁽¹⁾ | \$ 197,221 | \$ 351,225 | \$ 822,351 | \$ (95,007) | \$ — | \$ 1,275,790 |

| Nine Months Ended September 30, 2014 | LoyaltyOne | Epsilon | Card Services | Corporate/ Other | Eliminations | Total |
|--|-------------------|----------------|----------------------|-----------------------------|---------------------|--------------|
| (In thousands) | | | | | | |
| Revenues | \$ 1,009,037 | \$ 1,082,111 | \$ 1,741,384 | \$ 372 | \$ (15,713) | \$ 3,817,191 |
| Income (loss) before income taxes | 155,510 | 81,342 | 660,299 | (203,321) | — | 693,830 |
| Interest expense, net | 4,947 | (22) | 90,866 | 96,352 | — | 192,143 |
| Operating income (loss) | 160,457 | 81,320 | 751,165 | (106,969) | — | 885,973 |
| Depreciation and amortization | 67,501 | 110,479 | 40,876 | 5,843 | — | 224,699 |
| Stock compensation expense | 8,443 | 15,390 | 9,968 | 15,953 | — | 49,754 |
| Adjusted EBITDA ⁽¹⁾ | 236,401 | 207,189 | 802,009 | (85,173) | — | 1,160,426 |
| Less: securitization funding costs | — | — | 67,974 | — | — | 67,974 |
| Less: interest expense on deposits | — | — | 25,526 | — | — | 25,526 |
| Less: adjusted EBITDA attributable to non-controlling interest | 24,381 | — | — | — | — | 24,381 |
| Adjusted EBITDA, net ⁽¹⁾ | \$ 212,020 | \$ 207,189 | \$ 708,509 | \$ (85,173) | \$ — | \$ 1,042,545 |

⁽¹⁾ Adjusted EBITDA is a non-GAAP financial measure equal to net income, the most directly comparable financial measure based on GAAP, plus stock compensation expense, provision for income taxes, interest expense, net, depreciation and other amortization, amortization of purchased intangibles and regulatory settlement. Adjusted EBITDA, net is also a non-GAAP financial measure equal to adjusted EBITDA less securitization funding costs, interest expense on deposits and adjusted EBITDA attributable to the non-controlling interest. Adjusted EBITDA and adjusted EBITDA, net are presented in accordance with ASC 280 as they are the primary performance metrics utilized to assess performance of the segments.

19. NON-CASH FINANCING AND INVESTING ACTIVITIES

In September 2015, the Company purchased 30,000 treasury shares under the Company's stock repurchase program for an aggregate amount of \$7.6 million that had not settled as of September 30, 2015 and was included in accounts payable in the Company's unaudited condensed consolidated balance sheets.

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

The following discussion should be read in conjunction with the unaudited condensed consolidated financial statements and related notes thereto presented in this quarterly report and the consolidated financial statements and related notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2014, filed with the Securities and Exchange Commission, or SEC, on February 27, 2015.

2015 Highlights

For the nine months ended September 30, 2015, revenue increased 23% to \$4.7 billion and adjusted EBITDA, net increased 22% to \$1.3 billion as compared to the prior year period.

LoyaltyOne®

LoyaltyOne generates revenue primarily from our coalition loyalty program in Canada, the AIR MILES® Reward Program, and our ownership interest in BrandLoyalty Group B.V., or BrandLoyalty. Effective January 1, 2015, our ownership interest in BrandLoyalty increased from 60% to 70%.

Revenue for the LoyaltyOne segment decreased 2% to \$988.8 million and adjusted EBITDA, net decreased 7% to \$197.2 million for the nine months ended September 30, 2015, in each case as compared to the prior year period. The strengthening of the U.S. dollar against both the Euro and Canadian dollar negatively impacted revenue and adjusted EBITDA, net by approximately \$174.2 million and \$32.0 million, respectively.

Excluding foreign currency impacts, revenue and adjusted EBITDA net, increased by approximately 15% and 8%, respectively, due to growth from both our short-term and coalition loyalty programs. Our short-term loyalty programs have expanded into North America, currently operating in Canada, and with the potential to launch a U.S. pilot in 2016.

For the AIR MILES Reward Program, AIR MILES reward miles issued and AIR MILES reward miles redeemed are the two primary drivers of revenue and indicators of success of the program. The number of AIR MILES reward miles issued impacts the number of future AIR MILES reward miles available to be redeemed. This can also impact future revenue recognized with respect to the number of AIR MILES reward miles redeemed and the amount of breakage for those AIR MILES reward miles expected to remain unredeemed.

Within our coalition loyalty program, AIR MILES reward miles issued increased 11% due to the grocer vertical, driven by promotional activity and by the expansion of our relationship with Sobeys. AIR MILES reward miles redeemed increased 11% due to higher redemptions under our AIR MILES Cash program option. We have experienced strong promotional activity in particular from our grocer sponsors, but expect this to lessen in the fourth quarter and expect mid-single-digit issuance growth for the year.

During the nine months ended September 30, 2015, LoyaltyOne announced a multi-year contract renewal with Metro Ontario Inc., a national grocery retailer in Canada, which extends our partnership in the Ontario market. In addition, we announced an expansion of our relationship with Sobeys, another Canadian grocery retailer, to begin to issue AIR MILES reward miles at Sobeys, Sobeys Urban Fresh and Foodland stores across Ontario in 2015. We also announced a multi-year renewal of our agreement with Shell Canada Products as a sponsor in the AIR MILES Reward Program and signed a new multi-year agreement with Shell Canada Products, as the licensor and franchisor of the JiffyLube® brand in Canada, to allow AIR MILES reward miles to be issued at the more than 150 participating JiffyLube service centers throughout Canada. We also signed a new multi-year agreement with Lowe's Canada, a Canadian home improvement company, to become a sponsor in the AIR MILES Reward Program.

Additionally, on August 31, 2015, BrandLoyalty acquired all of the stock of Edison International Concept & Agencies B.V., or Edison, and Max Holding B.V., or Merison, two Netherlands-based loyalty marketers, for consideration of approximately \$45.4 million. The acquisition expands BrandLoyalty's short-term loyalty programs into new markets with new brands and is expected to have an immaterial impact to our results of operations for 2015.

Epsilon®

Revenue increased 42% to \$1.5 billion and adjusted EBITDA, net increased 70% to \$351.2 million for the nine months ended September 30, 2015, in each case as compared to the same period in 2014. These increases were primarily due to the acquisition of Conversant, Inc., or Conversant®, in December 2014, which added \$398.6 million and \$133.5 million of revenue and adjusted EBITDA, net, respectively, for the nine months ended September 30, 2015. Excluding Conversant, Epsilon's revenues increased \$51.8 million and adjusted EBITDA, net increased \$10.5 million, driven by database builds completed and placed in production for new clients and strength in the automotive vertical, both of which have offset some weakness within our agency offerings.

During the nine months ended September 30, 2015, Epsilon announced new multi-year agreements with Nature's Way, a dietary supplement brand, to serve as the digital agency of record across a number of brands and to provide CRM marketing services, and with Turner Broadcasting System, Inc., a Time Warner company, to provide analytics and data services to support the Turner Data Cloud infrastructure.

Card Services

In the first quarter of 2015, we renamed our Private Label Services and Credit segment to "Card Services," which had no impact to the reported results of the segment in the current or prior periods.

Revenue increased 26% to \$2.2 billion and adjusted EBITDA, net increased 16% to \$822.4 million for the nine months ended September 30, 2015, in each case as compared to the same period in 2014.

For the nine months ended September 30, 2015, average credit card and loan receivables increased 32% as compared to the same period in the prior year as a result of increased credit sales, recent client signings and recent credit card portfolio acquisitions. Credit sales increased 35% for the nine months ended September 30, 2015 due to cardholder growth, strong credit cardholder spending, recent client signings and recent credit card portfolio acquisitions.

During the nine months ended September 30, 2015, Card Services announced the signing of new multi-year agreements to provide co-brand credit card services to Red Roof Inn, a hotel chain; Cornerstone, a business unit of HSN, Inc.; Farmers Insurance, one of the largest multiline insurers in the U.S; and Univision Communications Inc., a media company. We also announced the renewal of multi-year agreements to continue providing private label credit card services to Talbots, Inc., a women's apparel retailer, and FULLBEAUTY Brands, a fashion and lifestyle resource for plus-size women. We also signed a new multi-year agreement to provide private label credit card services and assume management of an existing co-brand card program in the United States for Toyota, a leading automaker, and to acquire the existing co-brand credit card portfolio at a future date.

Critical Accounting Policies and Estimates

There have been no material changes to our critical accounting policies and estimates from the information provided in Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations," included in our Annual Report filed on Form 10-K for the fiscal year ended December 31, 2014.

Recently Issued Pronouncements

See "Recently Issued Accounting Standards" under Note 1, "Summary of Significant Accounting Policies," of the Notes to Unaudited Condensed Consolidated Financial Statements for a discussion of certain accounting standards that have been issued during 2014 and 2015.

Use of Non-GAAP Financial Measures

Adjusted EBITDA is a non-GAAP financial measure equal to net income, the most directly comparable financial measure based on accounting principles generally accepted in the United States of America, or GAAP, plus stock compensation expense, provision for income taxes, interest expense, net, depreciation and other amortization, amortization of purchased intangibles and regulatory settlement. Adjusted EBITDA, net is also a non-GAAP financial measure equal to adjusted EBITDA less securitization funding costs, interest expense on deposits and adjusted EBITDA attributable to the non-controlling interest.

We use adjusted EBITDA and adjusted EBITDA, net as an integral part of our internal reporting to measure the performance of our reportable segments and to evaluate the performance of our senior management. Adjusted EBITDA and adjusted EBITDA, net are each considered an important indicator of the operational strength of our businesses. Adjusted EBITDA eliminates the uneven effect across all business segments of considerable amounts of non-cash depreciation of tangible assets and amortization of intangible assets, including certain intangible assets that were recognized in business combinations. A limitation of this measure, however, is that it does not reflect the periodic costs of certain capitalized tangible and intangible assets used in generating revenues in our businesses. Management evaluates the costs of such tangible and intangible assets, such as capital expenditures, investment spending and return on capital and therefore the effects are excluded from adjusted EBITDA. Adjusted EBITDA also eliminates the non-cash effect of stock compensation expense.

Stock compensation expense and regulatory settlement are not included in the measurement of segment adjusted EBITDA provided to the chief operating decision maker for purposes of assessing segment performance and decision making with respect to resource allocations. In addition to the above, adjusted EBITDA, net also excludes the interest associated with financing our credit card and loan receivables, which represents securitization funding costs and interest on deposits, and the percentage of the adjusted EBITDA attributable to the non-controlling interest. We believe that adjusted EBITDA and adjusted EBITDA, net provide useful information to our investors regarding our performance and overall results of operations. Adjusted EBITDA and adjusted EBITDA, net are not intended to be performance measures that should be regarded as an alternative to, or more meaningful than, either operating income or net income as indicators of operating performance or to cash flows from operating activities as a measure of liquidity. In addition, adjusted EBITDA and adjusted EBITDA, net are not intended to represent funds available for dividends, reinvestment or other discretionary uses, and should not be considered in isolation or as a substitute for measures of performance prepared in accordance with GAAP.

The adjusted EBITDA and adjusted EBITDA, net measures presented in this Quarterly Report on Form 10-Q may not be comparable to similarly titled measures presented by other companies, and may not be identical to corresponding measures used in our various agreements.

| | Three Months Ended | | Nine Months Ended | |
|--|---------------------------|-------------------|--------------------------|---------------------|
| | September 30, | | September 30, | |
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands) | | | |
| Net income | \$ 130,382 | \$ 164,948 | \$ 425,253 | \$ 439,884 |
| Stock compensation expense | 21,813 | 18,257 | 73,343 | 49,754 |
| Provision for income taxes | 75,031 | 95,229 | 231,705 | 253,946 |
| Interest expense, net | 82,098 | 61,464 | 240,820 | 192,143 |
| Depreciation and other amortization | 36,450 | 28,070 | 104,983 | 79,555 |
| Amortization of purchased intangibles | 86,930 | 48,261 | 262,131 | 145,144 |
| Regulatory settlement | 64,563 | — | 64,563 | — |
| Adjusted EBITDA | 497,267 | 416,229 | 1,402,798 | 1,160,426 |
| Less: Securitization funding costs | 23,143 | 22,763 | 71,509 | 67,974 |
| Less: Interest expense on deposits | 13,719 | 9,064 | 37,099 | 25,526 |
| Less: Adjusted EBITDA attributable to non-controlling interest | 7,455 | 8,378 | 18,400 | 24,381 |
| Adjusted EBITDA, net | <u>\$ 452,950</u> | <u>\$ 376,024</u> | <u>\$ 1,275,790</u> | <u>\$ 1,042,545</u> |

Consolidated Results of Operations*Three months ended September 30, 2015 compared to the three months ended September 30, 2014*

| | Three Months Ended | | % Change |
|--|---------------------------|-------------------|---------------------|
| | September 30, | | |
| | 2015 | 2014 | 2015 to 2014 |
| (In thousands, except percentages) | | | |
| Revenues | | | |
| Transaction | \$ 83,126 | \$ 87,162 | (5)% |
| Redemption | 220,922 | 232,464 | (5) |
| Finance charges, net | 737,918 | 597,892 | 23 |
| Marketing services | 498,955 | 353,525 | 41 |
| Other revenue | 48,196 | 48,090 | — |
| Total revenue | <u>1,589,117</u> | <u>1,319,133</u> | <u>20%</u> |
| Operating expenses | | | |
| Cost of operations (exclusive of depreciation and amortization disclosed separately below) | 901,095 | 767,415 | 17 |
| Provision for loan loss | 171,678 | 114,577 | 50 |
| General and administrative | 40,890 | 39,169 | 4 |
| Regulatory settlement | 64,563 | — | 100 |
| Depreciation and other amortization | 36,450 | 28,070 | 30 |
| Amortization of purchased intangibles | 86,930 | 48,261 | 80 |
| Total operating expenses | <u>1,301,606</u> | <u>997,492</u> | <u>30%</u> |
| Operating income | 287,511 | 321,641 | (11)% |
| Interest expense | | | |
| Securitization funding costs | 23,143 | 22,763 | 2 |
| Interest expense on deposits | 13,719 | 9,064 | 51 |
| Interest expense on long-term and other debt, net | 45,236 | 29,637 | 53 |
| Total interest expense, net | <u>82,098</u> | <u>61,464</u> | <u>34</u> |
| Income before income tax | \$ 205,413 | \$ 260,177 | (21)% |
| Provision for income taxes | 75,031 | 95,229 | (21) |
| Net income | <u>\$ 130,382</u> | <u>\$ 164,948</u> | <u>(21)%</u> |
| Key Operating Metrics: | | | |
| Credit card statements generated | 60,025 | 52,319 | 15% |
| Credit sales | \$ 6,000,355 | \$ 4,479,375 | 34% |
| Average credit card and loan receivables | \$ 11,369,434 | \$ 8,736,664 | 30% |
| AIR MILES reward miles issued | 1,355,744 | 1,286,668 | 5% |
| AIR MILES reward miles redeemed | 1,061,336 | 992,761 | 7% |

Revenue. Total revenue increased \$270.0 million, or 20%, to \$1.6 billion for the three months ended September 30, 2015 from \$1.3 billion for the three months ended September 30, 2014. The net increase was due to the following:

- *Transaction.* Revenue decreased \$4.0 million, or 5%, to \$83.1 million for the three months ended September 30, 2015. AIR MILES reward miles issuance fees, for which we provide marketing and administrative services, decreased \$5.1 million as a result of the decline in the Canadian dollar relative to the U.S. dollar. In Canadian dollars, issuance fees increased due to the growth in issuance over the last several quarters. This decrease was offset in part by an increase in servicing fees charged to our credit cardholders.
- *Redemption.* Revenue decreased \$11.5 million, or 5%, to \$220.9 million for the three months ended September 30, 2015. Revenue was negatively impacted by the decline in both the Euro and Canadian dollar relative to the U.S. dollar, which resulted in a \$43.2 million decrease in revenue. This decrease was offset in part by the increase in loyalty programs in the market during the three months ended September 30, 2015.

- *Finance charges, net.* Revenue increased \$140.0 million, or 23%, to \$737.9 million for the three months ended September 30, 2015. This increase was driven by a 30% increase in average credit card and loan receivables, which increased revenue \$180.2 million through a combination of recent credit card portfolio acquisitions and strong cardholder spending. This increase was offset in part by a 140 basis point decline in finance charge yield, which decreased revenue by \$40.1 million. Our finance charge yield has been negatively impacted by the growth of our co-brand credit card programs.
- *Marketing Services.* Revenue increased \$145.4 million, or 41%, to \$499.0 million for the three months ended September 30, 2015. The increase in revenue was driven by the Conversant acquisition, which added \$129.3 million. Additionally, revenue increased \$17.5 million within our Epsilon segment due to database builds completed and placed into production for new clients as well as continued growth in services to existing clients and strength in the automotive vertical, all of which have offset some weakness within our agency offerings.

Cost of operations. Cost of operations increased \$133.7 million, or 17%, to \$901.1 million for the three months ended September 30, 2015 as compared to \$767.4 million for the three months ended September 30, 2014. The net increase resulted from the following:

- Within the LoyaltyOne segment, cost of operations decreased \$20.0 million, impacted by the decline in both the Euro and Canadian dollar relative to the U.S. dollar, which resulted in a \$45.1 million decrease in cost of operations. In local currency, cost of operations increased during this period as a result of the increase in the cost of redemptions due to the number of programs in the market as compared to the prior year period.
- Within the Epsilon segment, cost of operations increased \$109.7 million due to the Conversant acquisition, which added \$96.9 million. Excluding Conversant, cost of operations increased \$12.8 million due to an increase of \$7.7 million in direct expenses associated with the increase in revenue and an increase of \$5.1 million in payroll and benefits expense associated with the addition of associates to support growth.
- Within the Card Services segment, cost of operations increased by \$45.3 million as operating costs increased \$30.3 million due to increased credit card processing expenses resulting from higher volumes, and increased marketing expenses to support the growth in credit sales. Additionally, payroll and benefit expenses increased \$15.0 million due to an increase in the number of associates.

Provision for loan loss. Provision for loan loss increased \$57.1 million, or 50%, to \$171.7 million for the three months ended September 30, 2015 as compared to \$114.6 million for the three months ended September 30, 2014. The increase in the provision was driven by growth in our credit card and loan receivables, which increased by 27%, and an increase in the net principal loss rate.

General and administrative. General and administrative expenses increased \$1.7 million, or 4%, to \$40.9 million for the three months ended September 30, 2015 as compared to \$39.2 million for the three months ended September 30, 2014. Lower discretionary benefit costs and professional fees were offset by higher foreign currency exchange gains in the prior year period related to the contingent liability associated with the BrandLoyalty acquisition and the related foreign currency exchange forward contract.

Regulatory settlement. For the three months ended September 30, 2015, we incurred approximately \$64.6 million in expenses primarily associated with consent orders with the Federal Deposit Insurance Corporation, or FDIC, to provide restitution of approximately \$61.5 million to eligible customers and \$2.5 million in civil money penalties to the FDIC.

Depreciation and other amortization. Depreciation and other amortization increased \$8.4 million, or 30%, to \$36.5 million for the three months ended September 30, 2015, as compared to \$28.1 million for the three months ended September 30, 2014, due to additional assets placed into service resulting from both the Conversant acquisition and recent capital expenditures.

Amortization of purchased intangibles. Amortization of purchased intangibles increased \$38.7 million, or 80%, to \$86.9 million for the three months ended September 30, 2015 as compared to \$48.3 million for the three months ended September 30, 2014. The increase relates to \$41.9 million of additional amortization associated with the intangible assets from the Conversant acquisition.

Interest expense, net. Total interest expense, net increased \$20.6 million, or 34%, to \$82.1 million for the three months ended September 30, 2015 as compared to \$61.5 million for the three months ended September 30, 2014. The increase was due to the following:

- *Securitization funding costs.* Securitization funding costs increased \$0.4 million as higher average borrowings were offset in part by lower average interest rates.
- *Interest expense on deposits.* Interest expense on deposits increased \$4.6 million due to an increase in average borrowings with comparable average interest rates.
- *Interest expense on long-term and other debt, net.* Interest expense on long-term and other debt, net increased \$15.6 million, primarily due to an \$11.1 million increase associated with both the \$1.4 billion incremental term loan borrowed in December 2014 and the \$600.0 million Senior Notes due 2022 issued in July 2014 as well as a \$3.1 million increase related to additional borrowings on our revolving line of credit.

Taxes. Income tax expense decreased \$20.2 million to \$75.0 million for the three months ended September 30, 2015 from \$95.2 million for the three months ended September 30, 2014 due to a decrease in taxable income.

Nine months ended September 30, 2015 compared to the nine months ended September 30, 2014

| | Nine Months Ended September 30, | | % Change |
|--|--|-------------|---------------------|
| | 2015 | 2014 | 2015 to 2014 |
| (In thousands, except percentages) | | | |
| Revenues | | | |
| Transaction | \$ 263,195 | \$ 251,390 | 5% |
| Redemption | 747,192 | 744,658 | — |
| Finance charges, net | 2,101,360 | 1,672,339 | 26 |
| Marketing services | 1,435,520 | 1,021,813 | 40 |
| Other revenue | 143,625 | 126,991 | 13 |
| Total revenue | 4,690,892 | 3,817,191 | 23% |
| Operating expenses | | | |
| Cost of operations (exclusive of depreciation and amortization disclosed separately below) | 2,787,501 | 2,323,210 | 20 |
| Provision for loan loss | 461,944 | 281,811 | 64 |
| General and administrative | 111,992 | 101,498 | 10 |
| Regulatory settlement | 64,563 | — | 100 |
| Depreciation and other amortization | 104,983 | 79,555 | 32 |
| Amortization of purchased intangibles | 262,131 | 145,144 | 81 |
| Total operating expenses | 3,793,114 | 2,931,218 | 29% |
| Operating income | 897,778 | 885,973 | 1% |
| Interest expense | | | |
| Securitization funding costs | 71,509 | 67,974 | 5 |
| Interest expense on deposits | 37,099 | 25,526 | 45 |
| Interest expense on long-term and other debt, net | 132,212 | 98,643 | 34 |
| Total interest expense, net | 240,820 | 192,143 | 25 |
| Income before income tax | 656,958 | 693,830 | (5)% |
| Provision for income taxes | 231,705 | 253,946 | (9) |
| Net income | \$ 425,253 | \$ 439,884 | (3)% |

Key Operating Metrics:

| | | | |
|--|---------------|---------------|-----|
| Credit card statements generated | 177,920 | 154,448 | 15% |
| Credit sales | \$ 16,968,812 | \$ 12,591,188 | 35% |
| Average credit card and loan receivables | \$ 10,970,979 | \$ 8,309,963 | 32% |
| AIR MILES reward miles issued | 4,066,816 | 3,680,226 | 11% |
| AIR MILES reward miles redeemed | 3,416,116 | 3,087,839 | 11% |

Revenue. Total revenue increased \$873.7 million, or 23%, to \$4.7 billion for the nine months ended September 30, 2015 from \$3.8 billion for the nine months ended September 30, 2014. The increase was due to the following:

- *Transaction.* Revenue increased \$11.8 million, or 5%, to \$263.2 million for the nine months ended September 30, 2015 due to an increase in servicing fees charged to our credit cardholders. This increase was partially offset as AIR MILES reward miles issuance fees, for which we provide marketing and administrative services, decreased \$7.1 million due to the decline in the Canadian dollar relative to the U.S. dollar. In Canadian dollars, issuance fees increased due to the growth in issuance over the last several quarters.
- *Redemption.* Revenue increased \$2.5 million to \$747.2 million for the nine months ended September 30, 2015. Despite the impact of foreign currency exchange rates, which negatively impacted revenue by \$138.2 million, revenue increased due to a higher number of short-term loyalty programs in the market for the nine months ended September 30, 2015 as compared to the prior year period.

- *Finance charges, net.* Revenue increased \$429.0 million, or 26%, to \$2.1 billion for the nine months ended September 30, 2015 due to a 32% increase in average credit card and loan receivables, which increased revenue \$535.5 million. This increase was offset in part by a 130 basis point decline in finance charge yield, which decreased revenue by \$106.5 million. Our finance charge yield has been negatively impacted by the growth in our co-brand credit card programs.
- *Marketing services.* Revenue increased \$413.7 million, or 40%, to \$1.4 billion for the nine months ended September 30, 2015. The Conversant acquisition added \$373.7 million in revenue. Additionally, revenue increased \$46.1 million within our Epsilon segment due to database builds completed and placed into production for new clients and strength in the automotive vertical, both of which have offset some weakness within our agency offerings.
- *Other revenue.* Revenue increased \$16.6 million, or 13%, to \$143.6 million for the nine months ended September 30, 2015 due to the Conversant acquisition.

Cost of operations. Cost of operations increased \$464.3 million, or 20%, to \$2.8 billion for the nine months ended September 30, 2015 as compared to \$2.3 billion for the nine months ended September 30, 2014. The increase resulted from the following:

- Within the LoyaltyOne segment, cost of operations increased \$0.2 million due to an increase in the cost of redemptions associated with the increase in redemption revenue as discussed above, offset in part by the decline in both the Euro and Canadian dollar relative to the U.S. dollar, which resulted in a \$139.5 million decrease in cost of operations.
- Within the Epsilon segment, cost of operations increased \$328.2 million due primarily to the Conversant acquisition, which added \$285.8 million. The remaining increase is due to an increase in payroll and benefits expense of \$15.9 million associated with the addition of associates to support growth, including the onboarding of new clients, and an increase of \$26.3 million in direct processing expenses associated with the increase in revenue.
- Within the Card Services segment, cost of operations increased by \$140.0 million. Payroll and benefits expense increased \$37.3 million due to the addition of associates to support growth, and marketing expenses increased \$14.5 million to support the growth in credit sales. Other operating expenses increased \$88.2 million due to higher credit card processing costs associated with the increase in the number of statements generated and higher data processing expenses.

Provision for loan loss. Provision for loan loss increased \$180.1 million, or 64%, to \$461.9 million for the nine months ended September 30, 2015 as compared to \$281.8 million for the nine months ended September 30, 2014. The increase in the provision was driven by growth in our credit card and loan receivables and the turnover of credit card receivables acquired in 2014.

General and administrative. General and administrative expenses increased \$10.5 million, or 10%, to \$112.0 million for the nine months ended September 30, 2015 as compared to \$101.5 million for the nine months ended September 30, 2014, due to an increase in payroll expense and higher discretionary benefits.

Regulatory settlement. For the nine months ended September 30, 2015, we incurred approximately \$64.6 million in expenses primarily associated with consent orders with the FDIC to provide restitution of approximately \$61.5 million to eligible customers and \$2.5 million in civil money penalties to the FDIC.

Depreciation and other amortization. Depreciation and other amortization increased \$25.4 million, or 32%, to \$105.0 million for the nine months ended September 30, 2015 as compared to \$79.6 million for the nine months ended September 30, 2014, due to additional assets placed in service resulting from both the Conversant acquisition and recent capital expenditures.

Amortization of purchased intangibles. Amortization of purchased intangibles increased \$117.0 million, or 81%, to \$262.1 million for the nine months ended September 30, 2015 as compared to \$145.1 million for the nine months ended September 30, 2014. The increase relates to \$125.7 million of additional amortization associated with the intangible assets from the Conversant acquisition.

Interest expense, net. Total interest expense, net increased \$48.7 million, or 25%, to \$240.8 million for the nine months ended September 30, 2015 as compared to \$192.1 million for the nine months ended September 30, 2014. The increase was due to the following:

- *Securitization funding costs.* Securitization funding costs increased \$3.5 million, as higher average borrowings were offset in part by lower average interest rates.
- *Interest expense on deposits.* Interest expense on deposits increased \$11.6 million due to an increase in average borrowings, offset in part by lower average interest rates.
- *Interest expense on long-term and other debt, net.* Interest expense on long-term and other debt, net increased \$33.6 million as a result of a \$43.8 million increase in interest expense associated with both the \$1.4 billion incremental term loan borrowed in December 2014 and the \$600.0 million Senior Notes due 2022 issued in July 2014 as well as a \$4.0 million increase related to additional borrowings on our revolving line of credit. These increases were offset by a decrease in interest expense of \$17.5 million associated with the convertible senior notes that were repaid at maturity in May 2014.

Taxes. Income tax expense decreased \$22.2 million to \$231.7 million for the nine months ended September 30, 2015 from \$253.9 million for the nine months ended September 30, 2014 due to a decline in the effective tax rate as well as a decrease in taxable income. The effective tax rate for the nine months ended September 30, 2015 improved to 35.3% as compared to 36.6% for the nine months ended September 30, 2014, primarily due to a favorable state tax ruling and a lapse in an applicable statute of limitations.

Segment Revenue and Adjusted EBITDA, net

Three months ended September 30, 2015 compared to the three months ended September 30, 2014

| | Three Months Ended | | % Change |
|----------------------------------|---|---------------------|---------------------|
| | September 30, | | |
| | 2015 | 2014 | 2015 to 2014 |
| Revenue: | | | |
| | (In thousands, except percentages) | | |
| LoyaltyOne | \$ 299,143 | \$ 324,484 | (8)% |
| Epsilon | 532,448 | 377,554 | 41 |
| Card Services | 763,997 | 622,330 | 23 |
| Corporate/Other | 138 | 144 | nm |
| Eliminations | (6,609) | (5,379) | nm |
| Total | <u>\$ 1,589,117</u> | <u>\$ 1,319,133</u> | <u>20%</u> |
| Adjusted EBITDA, net (1): | | | |
| LoyaltyOne | \$ 64,491 | \$ 69,486 | (7)% |
| Epsilon | 135,035 | 84,295 | 60 |
| Card Services | 289,163 | 254,601 | 14 |
| Corporate/Other | (35,739) | (32,358) | 10 |
| Total | <u>\$ 452,950</u> | <u>\$ 376,024</u> | <u>20%</u> |

(1) Adjusted EBITDA, net is equal to net income, plus stock compensation expense, provision for income taxes, interest expense, net, depreciation and amortization, amortization of purchased intangibles and regulatory settlement, less securitization funding costs, interest expense on deposits and adjusted EBITDA attributable to the non-controlling interest. For a reconciliation of adjusted EBITDA, net to net income, the most directly comparable GAAP financial measure, see "Use of Non-GAAP Financial Measures" included in this report.

nm – not meaningful.

Revenue. Total revenue increased \$270.0 million, or 20%, to \$1.6 billion for the three months ended September 30, 2015 from \$1.3 billion for the three months ended September 30, 2014. The net increase was due to the following:

- *LoyaltyOne.* Revenue decreased \$25.3 million, or 8%, to \$299.1 million for the three months ended September 30, 2015. Revenue was negatively impacted by the decline in both the Euro and Canadian dollar relative to the U.S. dollar, which resulted in a \$58.9 million decrease in revenue. This decrease was offset in part by the increase in short-term loyalty programs in the market during the three months ended September 30, 2015 as compared to the prior year period.
- *Epsilon.* Revenue increased \$154.9 million, or 41%, to \$532.4 million for the three months ended September 30, 2015 due primarily to the Conversant acquisition, which added \$137.6 million. Revenue also increased due to the completion of database builds for new clients placed in production, as well as continued growth in services to existing clients and strength in the automotive vertical, all of which have offset some weakness within our agency offerings.
- *Card Services.* Revenue increased \$141.7 million, or 23%, to \$764.0 million for the three months ended September 30, 2015. Finance charges, net increased by \$140.0 million, driven by a 30% increase in average credit card and loan receivables, which was a result of recent portfolio acquisitions and strong cardholder spending. Other servicing fees charged to our credit cardholders increased \$1.9 million due to higher volumes.

Adjusted EBITDA, net. Adjusted EBITDA, net increased \$76.9 million, or 20%, to \$453.0 million for the three months ended September 30, 2015 from \$376.0 million for the three months ended September 30, 2014. The net increase was due to the following:

- *LoyaltyOne.* Adjusted EBITDA, net decreased \$5.0 million, or 7%, to \$64.5 million for the three months ended September 30, 2015. Adjusted EBITDA, net was negatively impacted by the decline in both the Euro and Canadian dollar relative to the U.S. dollar, which resulted in a \$12.8 million decrease in adjusted EBITDA, net, offset in part by the increase in short-term loyalty programs in the market during the three months ended September 30, 2015 as compared to the prior year period.
- *Epsilon.* Adjusted EBITDA, net increased \$50.7 million, or 60%, to \$135.0 million for the three months ended September 30, 2015. Adjusted EBITDA, net was positively impacted by the acquisition of Conversant, which contributed \$45.8 million, and new database builds placed into production.
- *Card Services.* Adjusted EBITDA, net increased \$34.6 million, or 14%, to \$289.2 million for the three months ended September 30, 2015. Adjusted EBITDA, net was positively impacted by the increase in finance charges, net, but offset in part by both an increase in operating expenses due to increased volumes and an increase in the provision for loan loss resulting from both an increase in credit card and loan receivables and an increase in the net loss rate.
- *Corporate/Other.* Adjusted EBITDA, net decreased \$3.4 million to a loss of \$35.7 million for the three months ended September 30, 2015 as lower discretionary benefit costs and professional fees were offset by higher foreign currency exchange gains in the prior year period related to the contingent liability associated with the BrandLoyalty acquisition and the related foreign currency exchange forward contract.

Nine months ended September 30, 2015 compared to the nine months ended September 30, 2014

| | Nine Months Ended September 30, | | % Change |
|---|--|---------------------|---------------------|
| | 2015 | 2014 | 2015 to 2014 |
| (In thousands, except percentages) | | | |
| Revenue: | | | |
| LoyaltyOne | \$ 988,755 | \$ 1,009,037 | (2)% |
| Epsilon | 1,532,521 | 1,082,111 | 42 |
| Card Services | 2,189,113 | 1,741,384 | 26 |
| Corporate/Other | 280 | 372 | nm |
| Eliminations | (19,777) | (15,713) | nm |
| Total | <u>\$ 4,690,892</u> | <u>\$ 3,817,191</u> | <u>23%</u> |
| Adjusted EBITDA, net ⁽¹⁾: | | | |
| LoyaltyOne | \$ 197,221 | \$ 212,020 | (7)% |
| Epsilon | 351,225 | 207,189 | 70 |
| Card Services | 822,351 | 708,509 | 16 |
| Corporate/Other | (95,007) | (85,173) | 12 |
| Total | <u>\$ 1,275,790</u> | <u>\$ 1,042,545</u> | <u>22%</u> |

⁽¹⁾ Adjusted EBITDA, net is equal to net income, plus stock compensation expense, provision for income taxes, interest expense, net, depreciation and amortization, amortization of purchased intangibles and regulatory settlement, less securitization funding costs, interest expense on deposits and adjusted EBITDA attributable to the non-controlling interest. For a reconciliation of adjusted EBITDA, net to net income, the most directly comparable GAAP financial measure, see "Use of Non-GAAP Financial Measures" included in this report.

nm – not meaningful.

Revenue. Total revenue increased \$873.7 million, or 23%, to \$4.7 billion for the nine months ended September 30, 2015 from \$3.8 billion for the nine months ended September 30, 2014. The net increase was due to the following:

- **LoyaltyOne.** Revenue decreased \$20.3 million, or 2%, to \$988.8 million for the nine months ended September 30, 2015. Revenue was negatively impacted by the decline in both the Euro and Canadian dollar relative to the U.S. dollar, which resulted in a \$174.2 million decrease in revenue. This decrease was offset in part by a greater number of short-term loyalty programs in the market during the nine months ended September 30, 2015 as compared to the prior year period.
- **Epsilon.** Revenue increased \$450.4 million, or 42%, to \$1.5 billion for the nine months ended September 30, 2015. The Conversant acquisition added \$398.6 million. Excluding the Conversant acquisition, Epsilon's revenue increased \$51.8 million as a result of the completion of database builds placed in production for new clients and strength in the automotive vertical, both of which have offset some weakness within our agency offerings.
- **Card Services.** Revenue increased \$447.7 million, or 26%, to \$2.2 billion for the nine months ended September 30, 2015. Finance charges, net increased by \$429.0 million, driven by a 32% increase in average credit card and loan receivables due to strong cardholder spending and new client signings. Other servicing fees charged to our credit cardholders increased \$19.5 million due to higher volumes.

Adjusted EBITDA, net. Adjusted EBITDA, net increased \$233.2 million, or 22%, to \$1.3 billion for the nine months ended September 30, 2015 from \$1.0 billion for the nine months ended September 30, 2014. The net increase was due to the following:

- **LoyaltyOne.** Adjusted EBITDA, net decreased \$14.8 million, or 7%, to \$197.2 million for the nine months ended September 30, 2015. Adjusted EBITDA, net was negatively impacted by the decline in both the Euro and Canadian dollar relative to the U.S. dollar, which resulted in a \$32.0 million decrease in adjusted EBITDA, net, offset in part by the number of short-term loyalty programs in the market as compared to the nine months ended September 30, 2014.

- *Epsilon*. Adjusted EBITDA, net increased \$144.0 million, or 70%, to \$351.2 million for the nine months ended September 30, 2015. The Conversant acquisition added \$133.5 million. Excluding the Conversant acquisition, adjusted EBITDA, net increased by \$10.5 million driven by database builds completed and placed in production for new clients.
- *Card Services*. Adjusted EBITDA, net increased \$113.8 million, or 16%, to \$822.4 million for the nine months ended September 30, 2015. Adjusted EBITDA, net was positively impacted by the increase in finance charges, net, but offset in part by both an increase in operating expenses due to increased volumes and an increase in the provision for loan loss due to the increase in credit card and loan receivables.
- *Corporate/Other*. Adjusted EBITDA, net decreased \$9.8 million to a loss of \$95.0 million for the nine months ended September 30, 2015 due primarily to an increase in payroll expense and higher discretionary benefits.

Asset Quality

Our delinquency and net charge-off rates reflect, among other factors, the credit risk of our credit card and loan receivables, the success of our collection and recovery efforts, and general economic conditions.

Delinquencies. A credit card account is contractually delinquent when we do not receive the minimum payment by the specified due date on the cardholder's statement. Our policy is to continue to accrue interest and fee income on all credit card accounts beyond 90 days, except in limited circumstances, until the credit card account balance and all related interest and other fees are paid or charged-off, typically at 180 days delinquent. When an account becomes delinquent, a message is printed on the credit cardholder's billing statement requesting payment. After an account becomes 30 days past due, a proprietary collection scoring algorithm automatically scores the risk of the account becoming further delinquent. The collection system then recommends a collection strategy for the past due account based on the collection score and account balance and dictates the contact schedule and collections priority for the account. If we are unable to make a collection after exhausting all in-house collection efforts, we may engage collection agencies and outside attorneys to continue those efforts.

The following table presents the delinquency trends of our credit card and loan receivables portfolio:

| | <u>September 30,</u> <u>2015</u> | <u>% of</u> <u>Total</u> | <u>December 31,</u> <u>2014</u> | <u>% of</u> <u>Total</u> |
|--|-------------------------------------|-----------------------------|------------------------------------|-----------------------------|
| | (In thousands, except percentages) | | | |
| Receivables outstanding – principal | \$ 11,297,882 | 100.0% | \$ 10,762,498 | 100.0% |
| Principal receivables balances contractually delinquent: | | | | |
| 31 to 60 days | 175,018 | 1.5% | 157,760 | 1.4% |
| 61 to 90 days | 113,360 | 1.0 | 93,175 | 0.9 |
| 91 or more days | 225,553 | 2.0 | 182,945 | 1.7 |
| Total | <u>\$ 513,931</u> | <u>4.5%</u> | <u>\$ 433,880</u> | <u>4.0%</u> |

Net Charge-Offs. Our net charge-offs include the principal amount of losses from cardholders unwilling or unable to pay their account balances, as well as bankrupt and deceased credit cardholders, less recoveries and exclude charged-off interest, fees and fraud losses. Charged-off interest and fees reduce finance charges, net while fraud losses are recorded as an expense. Credit card and loan receivables, including unpaid interest and fees, are charged-off at the end of the month during which an account becomes 180 days contractually past due, except in the case of customer bankruptcies or death. Credit card and loan receivables, including unpaid interest and fees, associated with customer bankruptcies or death are charged-off at the end of each month subsequent to 60 days after the receipt of notification of the bankruptcy or death, but in any case, not later than the 180-day contractual time frame.

The net charge-off rate is calculated by dividing net charge-offs of principal receivables for the period by the average credit card and loan receivables for the period. Average credit card and loan receivables represent the average balance of the cardholder receivables at the beginning of each month in the periods indicated. The following table presents our net charge-offs for the periods indicated:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|-------------------------------------|--------------|------------------------------------|--------------|
| | 2015 | 2014 | 2015 | 2014 |
| | (In thousands, except percentages) | | | |
| Average credit card receivables | \$ 11,369,434 | \$ 8,736,664 | \$ 10,970,979 | \$ 8,309,963 |
| Net charge-offs of principal receivables | 123,748 | 87,803 | 365,369 | 275,126 |
| Net charge-offs as a percentage of average credit card receivables | 4.4% | 4.0% | 4.4% | 4.4% |

See Note 4, "Credit Card and Loan Receivables," of the Notes to Unaudited Condensed Consolidated Financial Statements for additional information related to the securitization of our credit card receivables.

Liquidity and Capital Resources

Operating Activities. We generated cash flow from operating activities of \$1,031.2 million and \$968.0 million for the nine months ended September 30, 2015 and 2014, respectively. The increase in cash flow from operating activities during the nine months ended September 30, 2015 as compared to the prior year period is a result of non-cash charges to income, such as the increase in the provision for loan loss due to the increase in credit card receivables. Changes in the fair value of the contingent liability for the BrandLoyalty acquisition from the initial valuation are classified as an adjustment to cash flow from operating activities and, as such, the adjustment of \$99.6 million during the first quarter of 2015 negatively impacted our cash flow from operating activities. Increases in working capital, due primarily to the reduction of accounts payable and accrued expenses, also negatively impacted our cash flow from operating activities.

We utilize our cash flow from operating activities for ongoing business operations, repayments of our revolving line of credit or other debt, acquisitions and capital expenditures.

Investing Activities. Cash used in investing activities was \$1,103.0 million and \$1,862.8 million for the nine months ended September 30, 2015 and 2014, respectively. Significant components of investing activities are as follows:

- **Redemption settlement assets.** Cash decreased \$16.4 million and \$48.9 million for the nine months ended September 30, 2015 and 2014, respectively. The use of cash in the nine months ended September 30, 2014 was related to an increase in funding related to the change in breakage rate at December 31, 2013.
- **Restricted cash.** During the nine months ended September 30, 2014, we collected principal accumulation of \$316.5 million for the repayment of non-recourse borrowings of consolidated securitized debt that was repaid in October 2014.
- **Credit card and loan receivables, net.** Cash decreased \$913.8 million and \$633.3 million for the nine months ended September 30, 2015 and 2014, respectively, due to growth in credit card receivables associated with recent portfolio acquisitions and strong core cardholder spending.
- **Purchase of credit card portfolios.** During the nine months ended September 30, 2014, we paid \$379.6 million to acquire two co-brand credit card portfolios.
- **Proceeds from the sale of credit card portfolio.** During the nine months ended September 30, 2015, we sold a credit card portfolio, resulting in proceeds of approximately \$26.9 million.
- **Payments for acquired business, net of cash acquired.** During the nine months ended September 30, 2015, we acquired two Netherlands-based loyalty marketing businesses for approximately \$45.4 million. During the nine months ended September 30, 2014, we utilized cash of \$259.5 million for the acquisition of our 60% ownership interest in BrandLoyalty on January 2, 2014.
- **Capital expenditures.** Cash paid for capital expenditures was \$140.1 million and \$114.6 million for the nine months ended September 30, 2015 and 2014, respectively. We anticipate capital expenditures to continue to be approximately 3% of annual revenue.
- **Purchases of other investments.** During the nine months ended September 30, 2014, we purchased \$100.1 million of U.S. Treasury bonds.

Financing Activities. Cash used in financing activities was \$7.1 million for the nine months ended September 30, 2015, compared to cash provided by financing activities of \$564.8 million for the nine months ended September 30, 2014. For the nine months ended September 30, 2015, the primary uses of cash were to acquire treasury shares of \$856.9 million, settle the BrandLoyalty contingent liability of \$205.9 million and acquire the additional 10% ownership in BrandLoyalty for \$87.4 million. These uses were partially offset by the issuance of the new term loan of \$200.0 million in September 2015 and borrowings under our debt agreements. For the nine months ended September 30, 2014, cash provided by financing activities was primarily from new borrowings, including the \$600.0 million issuance of senior notes due 2022 in July 2014.

Liquidity Sources. In addition to cash generated from operating activities, our primary sources of liquidity include our credit card securitization program, deposits issued by Comenity Bank and Comenity Capital Bank, our credit agreements and issuances of debt and equity securities. In addition to our efforts to renew and expand our current liquidity sources, we continue to seek new funding sources. We continue to expand our certificates of deposit and our money market deposits to supplement liquidity for our credit card and loan receivables.

Quantitative measures established by regulations to ensure capital adequacy require Comenity Bank and Comenity Capital Bank to maintain minimum amounts and ratios of Common Equity Tier 1, Tier 1 and total capital to risk weighted assets, and of Tier 1 capital to average assets. The Common Equity Tier 1 risk-based ratio, Tier 1 risk-based ratio, total risk-based capital ratio and Tier 1 leverage ratio for Comenity Bank were 16.5%, 16.5%, 17.8% and 15.6%, respectively, at September 30, 2015. The Common Equity Tier 1 risk-based ratio, Tier 1 risk-based ratio, total risk-based capital ratio and Tier 1 leverage ratio for Comenity Capital Bank were 13.7%, 13.7%, 15.0% and 13.8%, respectively, at September 30, 2015. Comenity Bank and Comenity Capital Bank are considered well capitalized.

We believe that internally generated funds and other sources of liquidity discussed above will be sufficient to meet working capital needs, capital expenditures, and other business requirements for at least the next 12 months.

As of September 30, 2015, we were in compliance with our debt covenants.

2013 Credit Facility. In September 2015, we amended our credit agreement, or the 2013 Credit Facility, and borrowed incremental term loans in the aggregate principal amount of \$200.0 million that mature on September 23, 2016. These term loans bear interest at the same rates and are generally subject to the same terms as the existing term loans under the 2013 Credit Facility. Subsequent to the amendment, our 2013 Credit Facility provides for \$2.85 billion in term loans, subject to certain principal repayments, and a \$1.3 billion revolving line of credit.

As of September 30, 2015, we had \$749.0 million outstanding under the 2013 Credit Facility and total availability of \$551.0 million. Our total leverage ratio, as defined in our credit agreement, was 2.7 to 1 at September 30, 2015, as compared to the maximum covenant ratio of 3.5 to 1.

BrandLoyalty Credit Agreement. In August 2015, BrandLoyalty amended its credit agreement. The BrandLoyalty credit agreement, as amended, provides for a committed revolving line of credit of €62.5 million and an uncommitted revolving line of credit of €62.5 million, both of which are scheduled to mature on August 25, 2018. As of September 30, 2015, the amount outstanding under the BrandLoyalty credit agreement was €103.2 million (\$115.3 million).

Securitization Program. We sell a majority of the credit card receivables originated by Comenity Bank to WFN Credit Company, LLC, which in turn sells them to World Financial Network Credit Card Master Trust, or Master Trust I, World Financial Network Credit Card Master Note Trust and World Financial Network Credit Card Master Trust III, or collectively, the WFN Trusts, as part of our credit card securitization program, which has been in existence since January 1996. We also sell our credit card receivables originated by Comenity Capital Bank to World Financial Capital Credit Company, LLC, which in turn sells them to World Financial Capital Master Note Trust, or the WFC Trust. These securitization programs are the primary vehicle through which we finance Comenity Bank's and Comenity Capital Bank's credit card receivables.

As of September 30, 2015, the WFN Trusts and the WFC Trust had approximately \$8.6 billion of securitized credit card receivables. Securitizations require credit enhancements in the form of cash, spread deposits, additional receivables and subordinated classes. The credit enhancement is principally based on the outstanding balances of the series issued by the WFN Trusts and the WFC Trust and by the performance of the credit card receivables in these credit card securitization trusts.

At September 30, 2015, we had \$5.0 billion of non-recourse borrowings of consolidated securitization entities, of which \$1.2 billion is due within the next 12 months. As of September 30, 2015, total capacity under the conduit facilities was \$2.1 billion, of which \$1.0 billion had been drawn and was included in non-recourse borrowings of consolidated securitization entities in the unaudited condensed consolidated balance sheets.

Historically, we have used both public and private term asset-backed securitization transactions as well as private conduit facilities as sources of funding for our credit card receivables. Private conduit facilities have been used to accommodate seasonality needs and to bridge to completion of asset-backed securitization transactions.

We have secured and continue to secure the necessary commitments to fund our portfolio of securitized credit card receivables originated by Comenity Bank and Comenity Capital Bank. However, certain of these commitments are short-term in nature and subject to renewal. There is not a guarantee that these funding sources, when they mature, will be renewed on similar terms or at all as they are dependent on the asset-backed securitization markets at the time.

In April 2015, Master Trust I issued \$500.0 million of asset-backed term notes, \$140.0 million of which were retained and eliminated from the unaudited condensed consolidated financial statements. These securities mature in April 2018 and have a variable interest rate equal to the London Interbank Offered Rate plus a margin of 0.48%.

In April 2015, we amended our 2009-VFN conduit facility, extending the maturity to March 31, 2017. In May 2015, we renewed our 2009-VFC1 conduit facility, increasing its capacity from \$440.0 million to \$900.0 million and extending the maturity to May 1, 2017.

In June 2015, \$450.0 million of Series 2010-A asset-backed term notes, \$56.2 million of which were retained by us and eliminated from the unaudited condensed consolidated financial statements, matured and were repaid.

In August 2015, Master Trust I issued \$625.0 million of asset-backed term notes, \$150.0 million of which were retained and eliminated from the unaudited condensed consolidated financial statements. These securities mature in August 2020 and have a fixed interest rate of 2.55%.

In September 2015, \$394.7 million of Series 2014-B asset-backed term notes, \$94.7 million of which were retained by us and eliminated from the unaudited condensed consolidated financial statements, matured and were repaid.

In October 2015, Master Trust I issued \$389.6 million of asset-backed term notes, \$89.6 million of which were retained by us and eliminated from the unaudited condensed consolidated financial statements. These securities mature in May 2017 and have a fixed interest rate of 1.26%.

The following table shows the maturities of borrowing commitments as of September 30, 2015 for the WFN Trusts and the WFC Trust by year:

| | <u>2015</u> | <u>2016</u> | <u>2017</u> | <u>2018</u> | <u>2019 and Thereafter</u> | <u>Total</u> |
|--------------------|-----------------------|---------------------|---------------------|-------------------|--------------------------------|---------------------|
| | (In thousands) | | | | | |
| Term notes | \$ — | \$ 1,050,000 | \$ 650,000 | \$ 991,000 | \$ 1,277,166 | \$ 3,968,166 |
| Conduit facilities | | | | | | |
| (1) | — | 450,000 | 1,600,000 | — | — | 2,050,000 |
| Total (2) | \$ — | \$ 1,500,000 | \$ 2,250,000 | \$ 991,000 | \$ 1,277,166 | \$ 6,018,166 |

(1) Amount represents borrowing capacity, not outstanding borrowings.

(2) Total amounts do not include \$1.6 billion of debt issued by the credit card securitization trusts, which was retained by us and has been eliminated in the unaudited condensed consolidated financial statements.

Early amortization events as defined within each asset-backed securitization transaction are generally driven by asset performance. We do not believe it is reasonably likely for an early amortization event to occur due to asset performance. However, if an early amortization event were declared, the trustee of the particular credit card securitization trust would retain the interest in the receivables along with the excess interest income that would otherwise be paid to our bank subsidiary until the credit card securitization investors were fully repaid. The occurrence of an early amortization event would significantly limit or negate our ability to securitize additional credit card receivables.

See Note 9, "Debt," of the Notes to Unaudited Condensed Consolidated Financial Statements for additional information regarding our debt.

Repurchase of Equity Securities. During the nine months ended September 30, 2015, we repurchased approximately 3.1 million shares of our common stock for an aggregate amount of \$864.5 million.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Market Risk

Market risk is the risk of loss from adverse changes in market prices and rates. Our primary market risks include interest rate risk, credit risk, foreign currency exchange rate risk and redemption reward risk.

There has been no material change from our Annual Report on Form 10-K for the year ended December 31, 2014 related to our exposure to market risk from interest rate risk, credit risk, foreign currency exchange rate risk and redemption reward risk.

Item 4. Controls and Procedures.

Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures

As of September 30, 2015, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-15 of the Securities Exchange Act of 1934. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that as of September 30, 2015 (the end of our third fiscal quarter), our disclosure controls and procedures are effective. Disclosure controls and procedures are controls and procedures designed to ensure that information required to be disclosed in our reports filed or submitted under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and include controls and procedures designed to ensure that information we are required to disclose in such reports is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

There have been no changes in our internal control over financial reporting that occurred during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

FORWARD-LOOKING STATEMENTS

This Form 10-Q and the documents incorporated by reference herein contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Such statements may use words such as "anticipate," "believe," "continue," "could," "estimate," "expect," "intend," "may," "predict," "project," "would" and similar expressions as they relate to us or our management. When we make forward-looking statements, we are basing them on our management's beliefs and assumptions, using information currently available to us. Although we believe that the expectations reflected in the forward-looking statements are reasonable, these forward-looking statements are subject to risks, uncertainties and assumptions, including those discussed in the "Risk Factors" section in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2014, Item 1A of Part II of this Quarterly Report and any subsequent filings we make with the SEC.

If one or more of these or other risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, actual results may vary materially from what we projected. Any forward-looking statements contained in this quarterly report reflect our current views with respect to future events and are subject to these and other risks, uncertainties and assumptions relating to our operations, results of operations, growth strategy and liquidity. We have no intention, and disclaim any obligation, to update or revise any forward-looking statements, whether as a result of new information, future results or otherwise, except as required by law.

PART II

Item 1. Legal Proceedings.

From time to time we are involved in various claims and lawsuits arising in the ordinary course of our business that we believe will not have a material adverse effect on our business or financial condition, including claims and lawsuits alleging breaches of our contractual obligations. See Note 12, "Commitments and Contingencies," of the Notes to Unaudited Condensed Consolidated Financial Statements for additional information.

Item 1A. Risk Factors.

Other than as set forth below, there have been no material changes to the Risk Factors previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2014 or our Quarterly Reports on Form 10-Q for the quarters ended March 31, 2015 or June 30, 2015.

Current and proposed regulation and legislation relating to our card services could limit our business activities, product offerings and fees charged and may have a significant impact on our business, results of operations and financial condition.

On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") was enacted into law. The Dodd-Frank Act, among other things, includes a sweeping reform of the regulation and supervision of financial institutions, as well as of the regulation of derivatives and capital market activities.

The full impact of the Dodd-Frank Act is difficult to assess because many provisions require federal agencies to adopt implementing regulations, and some of the final implementing regulations have not yet been issued. In addition, the Dodd-Frank Act mandates multiple studies, which could result in future legislative or regulatory action. In particular, the Government Accountability Office issued its study on whether it is necessary, in order to strengthen the safety and soundness of institutions or the stability of the financial system of the United States, to eliminate the exemptions to the definition of "bank" under the Bank Holding Company Act for certain institutions including limited purpose credit card banks and industrial loan companies. The study did not recommend the elimination of these exemptions. However, if legislation were enacted to eliminate these exemptions without any grandfathering of or accommodations for existing institutions, we could be required to become a bank holding company and cease certain of our activities that are not permissible for bank holding companies or divest our credit card bank subsidiary, Comenity Bank, or our industrial bank subsidiary, Comenity Capital Bank.

The Dodd-Frank Act created a Consumer Financial Protection Bureau ("CFPB"), a new federal consumer protection regulator with authority to make further changes to the federal consumer protection laws and regulations. It is unclear what changes will be promulgated by the CFPB and what effect, if any, such changes would have on our business and operations. The CFPB assumed rulemaking authority under the existing federal consumer financial protection laws, and will enforce those laws against and examine certain non-depository institutions and insured depository institutions with total assets greater than \$10 billion and their affiliates.

While the CFPB does not examine Comenity Bank and Comenity Capital Bank, it will receive information from their primary federal regulator. In addition, the CFPB's broad rulemaking authority is expected to impact their operations. For example, the CFPB's rulemaking authority may allow it to change regulations adopted in the past by other regulators including regulations issued under the Truth in Lending Act or the Credit Card Accountability Responsibility and Disclosure Act of 2009 (the "CARD Act") by the Board of Governors of the Federal Reserve System. The CFPB's ability to rescind, modify or interpret past regulatory guidance could increase our compliance costs and litigation exposure. Furthermore, the CFPB has broad authority to prevent "unfair, deceptive or abusive" acts or practices and has taken enforcement action against other credit card issuers and financial services companies. Evolution of these standards could result in changes to pricing, practices, procedures and other activities relating to our credit card accounts in ways that could reduce the associated return. It is unclear what changes would be promulgated by the CFPB and what effect, if any, such changes would have on our credit accounts.

The Dodd-Frank Act authorizes certain state officials to enforce regulations issued by the CFPB and to enforce the Dodd-Frank Act's general prohibition against unfair, deceptive or abusive practices. To the extent that states enact requirements that differ from federal standards or courts adopt interpretations of federal consumer laws that differ from those adopted by the federal banking agencies, we may be required to alter products or services offered in some jurisdictions or cease offering products, which will increase compliance costs and reduce our ability to offer the same products and services to consumers nationwide.

Various federal and state laws and regulations significantly limit the retail credit card services activities in which we are permitted to engage. Such laws and regulations, among other things, limit the fees and other charges that we can impose on consumers, limit or proscribe certain other terms of our products and services, require specified disclosures to consumers, or require that we maintain certain licenses, qualifications and minimum capital levels. In some cases, the precise application of these statutes and regulations is not clear. In addition, numerous legislative and regulatory proposals are advanced each year which, if adopted, could have a material adverse effect on our profitability or further restrict the manner in which we conduct our activities. The CARD Act, which was enacted in May 2009 and together with its implementing rules, became effective in 2010, acts to limit or modify certain credit card practices and require increased disclosures to consumers. The credit card practices addressed by the rules include, but are not limited to, restrictions on the application of rate increases to existing and new balances, payment allocation, default pricing, imposition of late fees and two-cycle billing. The failure to comply with, or adverse changes in, the laws or regulations to which our business is subject, or adverse changes in their interpretation, could have a material adverse effect on our ability to collect our receivables and generate fees on the receivables, thereby adversely affecting our profitability.

In the normal course of business, from time to time, Comenity Bank and Comenity Capital Bank have been named as defendants in various legal actions, including arbitrations, class actions and other litigation arising in connection with their business activities. While historically the arbitration provision in each bank's customer agreement has generally limited such bank's exposure to consumer class action litigation, there can be no assurance that the banks will be successful in enforcing the arbitration clause in the future. There may also be legislative, administrative or regulatory efforts to directly or indirectly prohibit the use of pre-dispute arbitration clauses. Recently, the CFPB publicly announced that it is considering proposing rules that would ban consumer financial companies from using arbitration clauses that limit a consumer's right to participate in class action litigation.

Comenity Bank and Comenity Capital Bank are also involved, from time to time, in reviews, investigations, and proceedings (both formal and informal) by governmental agencies regarding the bank's business, which could subject the bank to significant fines, penalties, obligations to change its business practices or other requirements. For example, in September 2015, each bank entered into a consent order with the FDIC agreeing to collectively provide restitution of approximately \$61.5 million to eligible customers, to pay \$2.5 million in civil money penalties to the FDIC and to make further enhancements to their compliance and other processes related to the marketing, promotion and sale of add-on products.

The effect of the Dodd-Frank Act on our business and operations could be significant, depending upon final implementing regulations, the actions of our competitors and the behavior of other marketplace participants. In addition, we may be required to invest significant management time and resources to address the various provisions of the Dodd-Frank Act and the numerous regulations that are required to be issued under it. The Dodd-Frank Act and any related legislation or regulations may have a material impact on our business, results of operations and financial condition.

Legislation relating to consumer privacy may affect our ability to collect data that we use in providing our loyalty and marketing services, which, among other things, could negatively affect our ability to satisfy our clients' needs.

The enactment of new or amended legislation or industry regulations pertaining to consumer or private sector privacy issues could have a material adverse impact on our marketing services. Legislation or industry regulations regarding consumer or private sector privacy issues could place restrictions upon the collection, sharing and use of information that is currently legally available, which could materially increase our cost of collecting some data. These types of legislation or industry regulations could also prohibit us from collecting or disseminating certain types of data, which could adversely affect our ability to meet our clients' requirements and our profitability and cash flow targets. While 48 states and the District of Columbia have enacted data breach notification laws, there is no such federal law generally applicable to our businesses. Data breach notification legislation has been proposed widely and exists in specific countries and jurisdictions in which we conduct business. If enacted, these legislative measures could impose strict requirements on reporting time frames for providing notice, as well as the contents of such notices. In addition to the United States, Canadian and European Union regulations discussed below, we have expanded our marketing services through the acquisition of companies formed and operating in foreign jurisdictions that may be subject to additional or more stringent legislation and regulations regarding consumer or private sector privacy.

In the United States, federal and state laws such as the federal Gramm-Leach-Bliley Act and the Fair Credit Reporting Act, as amended by the Fair and Accurate Credit Transactions Act of 2003, make it more difficult to collect, share and use information that has previously been legally available and may increase our costs of collecting some data. Regulations under these acts give cardholders the ability to "opt out" of having information generated by their credit card purchases shared with other affiliated and unaffiliated parties or the public. Our ability to gather, share and utilize this data will be adversely affected if a significant percentage of the consumers whose purchasing behavior we track elect to "opt out," thereby precluding us and our affiliates from using their data.

In the United States, the federal Do-Not-Call Implementation Act makes it more difficult to telephonically communicate with prospective and existing customers. Similar measures were implemented in Canada beginning September 1, 2008. Regulations in both the United States and Canada give consumers the ability to "opt out," through a national do-not-call registry and state do-not-call registries of having telephone solicitations placed to them by companies that do not have an existing business relationship with the consumer. In addition, regulations require companies to maintain an internal do-not-call list for those who do not want the companies to solicit them through telemarketing. These regulations could limit our ability to provide services and information to our clients. Failure to comply with these regulations could have a negative impact on our reputation and subject us to significant penalties. Further, the Federal Communications Commission has approved interpretations of rules related to the Telephone Consumer Protection Act defining robo-calls, which may affect our ability to contact customers and may increase our litigation exposure.

In the United States, the federal Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003 restricts our ability to send commercial electronic mail messages, the primary purpose of which is advertising or promoting a commercial product or service, to our customers and prospective customers. The act requires that a commercial electronic mail message provide the customers with an opportunity to opt-out from receiving future commercial electronic mail messages from the sender. Failure to comply with the terms of this act could have a negative impact on our reputation and subject us to significant penalties.

In Canada, the Personal Information Protection and Electronic Documents Act requires an organization to obtain a consumer's consent to collect, use or disclose personal information. Under this act, consumer personal information may be used only for the purposes for which it was collected. We allow our customers to voluntarily "opt out" from receiving either one or both promotional and marketing mail or promotional and marketing electronic mail. Heightened consumer awareness of, and concern about, privacy may result in customers "opting out" at higher rates than they have historically. This would mean that a reduced number of customers would receive bonus and promotional offers and therefore those customers may collect fewer AIR MILES reward miles.

Canada's Anti-Spam Legislation may restrict our ability to send commercial "electronic messages," defined to include text, sound, voice and image messages to email, or similar accounts, where the primary purpose is advertising or promoting a commercial product or service to our customers and prospective customers. The Act requires, in part, that a sender have consent to send a commercial electronic message, and provide the customers with an opportunity to opt out from receiving future commercial electronic email messages from the sender. Failure to comply with the terms of this Act or any proposed regulations that may be adopted in the future could have a negative impact on our reputation and subject us to significant monetary penalties.

In the European Union, the Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 requires member states to implement and enforce a comprehensive data protection law that is based on principles designed to safeguard personal data, defined as any information relating to an identified or identifiable natural person. The Directive frames certain requirements for transfer outside of the European Economic Area and individual rights such as consent requirements. The Directive may be superseded by the General Data Protection Regulation proposed in January 2012 which would create one standard for the European Union member states but could limit our ability to provide services and information to our customers. In October 2015, the Court of Justice of the European Union ruled that the EU-U.S. Safe Harbor Framework enabling transfers of personal data between the EU and the U.S. is invalid, which may affect our ability to transfer data out of the EU in providing service for our customers.

There is also rapid development of new privacy laws and regulations in the Asia Pacific region and elsewhere around the globe, including amendments of existing data protection laws to the scope of such laws and penalties for noncompliance. Failure to comply with these international data protection laws and regulations could have a negative impact on our reputation and subject us to significant penalties.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

The following table presents information with respect to purchases of our common stock made during the three months ended September 30, 2015:

| Period | Total Number of Shares Purchased ⁽¹⁾ | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs ⁽²⁾ |
|-----------------------|---|------------------------------|--|---|
| (Dollars in millions) | | | | |
| During 2015: | | | | |
| July 1-31 | 306,940 | \$ 278.39 | 300,907 | \$ 217.6 |
| August 1-31 | 120,205 | 261.60 | 115,000 | 187.5 |
| September 1-30 | 207,852 | 253.49 | 205,000 | 135.5 |
| Total | 634,997 | \$ 267.06 | 620,907 | \$ 135.5 |

(1) During the period represented by the table, 14,090 shares of our common stock were purchased by the administrator of our 401(k) and Retirement Savings Plan for the benefit of the employees who participated in that portion of the plan.

(2) On January 1, 2015, our Board of Directors authorized a stock repurchase program to acquire up to \$600.0 million of our outstanding common stock from January 1, 2015 through December 31, 2015. On April 15, 2015, our Board of Directors authorized an increase to the stock repurchase program originally approved on January 1, 2015 to acquire up to \$1.0 billion of our outstanding common stock through December 31, 2015. The stock repurchase plan is subject to any restrictions pursuant to the terms of our credit agreements, indentures, applicable securities laws or otherwise.

Item 3. Defaults Upon Senior Securities.

None

Item 4. Mine Safety Disclosures.

Not applicable.

Item 5. Other Information.*(a) Dismissal of Delaware Litigation; Fee and Expense Application Hearing*

The Company, as well as Conversant and the former directors of Conversant, was named as a defendant in In Re Conversant, Inc. Stockholder Litigation, C.A. No. 10174-VCL, the Court of Chancery of the State of Delaware. In November of 2014, the parties entered into a memorandum of understanding to preliminarily resolve the Delaware litigation. The plaintiffs in this consolidated action, who had sued on behalf of a putative class of Conversant shareholders (the "Class"), have elected not to seek final approval of that settlement, dismissed their claims against all defendants (which the Court granted with prejudice as to the Delaware plaintiffs on October 22, 2015), and have indicated that they intend to submit an application for an award of attorney's fees and reimbursement of expenses (the "Fee and Expense Application") in connection with certain disclosure claims that they believe plaintiffs caused to be mooted through certain disclosures made by the Company and Conversant in connection with the preliminary settlement. The Court has scheduled a hearing (the "Fee and Expense Application Hearing") to be held on February 10, 2016 at 2:00 p.m. in the New Castle County Courthouse, located at 500 North King Street, Wilmington, DE 19801 to: (a) consider the application by the plaintiffs' counsel for attorneys' fees and expenses; (b) hear and determine any objections to the Fee and Expense Application; and (c) rule on such other matters as the Court may deem appropriate. The defendants have reserved all rights to oppose any such Fee and Expense Application.

Any member of the Class who objects to the Fee and Expense Application, or who otherwise, wishes to be heard may appear in person or by such member's attorney at the Fee and Expense Application Hearing and present evidence or argument that may be proper and relevant; provided, however, that except for good cause shown, no person shall be heard and no papers, briefs, pleadings or other documents submitted by any person shall be considered by the Court unless not later than fourteen (14) calendar days prior to the Fee and Expense Application Hearing such person files with the Court and serves upon counsel listed below: (a) a written notice of intention to appear; (b) a statement of such person's objections to any matters before the Court; and (c) the grounds for such objections and the reasons that such person desires to appear and be heard, documentation evidencing membership in the Class as well as documents or writings such person desires the Court to consider. Such filings shall be filed with the Court and served upon the following counsel:

Raymond J. DiCamillo, Esq.
RICHARDS, LAYTON & FINGER, P.A.
920 North King Street
Wilmington, Delaware 19801

- and to -

Frank A. Bottini, Esq.
BOTTINI & BOTTINI, INC.
7817 Ivanhoe Ave., Suite 102
La Jolla, CA 92037

Unless the Court otherwise directs, no person shall be entitled to object to the approval of the Fee and Expense Application, any judgment entered thereon, or otherwise be heard, except by serving and filing a written objection and supporting papers and documents as described in the preceding paragraph. Any person who fails to object in the manner described above shall be deemed to have waived the right to object (including any right of appeal) and shall be forever barred from raising such objection in this or any other action or proceeding.

Item 6. Exhibits.

(a) Exhibits:

EXHIBIT INDEX

| Exhibit No. | Filer | Description | Incorporated by Reference | | |
|--------------------|-------------------|---|----------------------------------|----------------|--------------------|
| | | | Form | Exhibit | Filing Date |
| 3.1 | (a) | Second Amended and Restated Certificate of Incorporation of the Registrant. | S-1 | 3.1 | 3/3/00 |
| 3.2 | (a) | Certificate of Amendment to the Second Amended and Restated Certificate of Incorporation of the Registrant. | 8-K | 3.1 | 6/7/13 |
| 3.3 | (a) | Fourth Amended and Restated Bylaws of the Registrant. | 8-K | 3.2 | 6/7/13 |
| 4 | (a) | Specimen Certificate for shares of Common Stock of the Registrant. | 10-Q | 4 | 8/8/03 |
| 10.1 | (b) (c) (d) | Series 2015-B Indenture Supplement, dated as of August 21, 2015, between World Financial Network Credit Card Master Note Trust and MUFG Union Bank, N.A. | 8-K | 4.1 | 8/25/15 |
| 10.2 | (a) | Amendment and Restatement Agreement, dated as of August 25, 2015, including Amended and Restated Facilities Agreement, as amended, by and among Brand Loyalty Group B.V. and certain subsidiaries parties thereto, as borrowers and guarantors, Deutsche Bank Nederland N.V. (as Arranger) and ING Bank N.V. (as Arranger, Agent and Security Agent). | 8-K | 10.1 | 8/28/15 |
| 10.3 | (a) | Second Amendment to Credit Agreement, dated as of September 25, 2015, by and among Alliance Data Systems Corporation, as borrower, and certain of its subsidiaries as guarantors, Wells Fargo Bank, N.A., as Administrative Agent and Letter of Credit Issuer, and various other lenders. | 8-K | 10.1 | 9/29/15 |
| 10.4 | (b) (c) (d) | Series 2015-C Indenture Supplement, dated as of October 27, 2015, between World Financial Network Credit Card Master Note Trust and MUFG Union Bank, N.A. | 8-K | 4.1 | 10/29/15 |
| *31.1 | (a) | Certification of Chief Executive Officer of Alliance Data Systems Corporation pursuant to Rule 13a-14(a) promulgated under the Securities Exchange Act of 1934, as amended. | | | |
| *31.2 | (a) | Certification of Chief Financial Officer of Alliance Data Systems Corporation pursuant to Rule 13a-14(a) promulgated under the Securities Exchange Act of 1934, as amended. | | | |
| *32.1 | (a) | Certification of Chief Executive Officer of Alliance Data Systems Corporation pursuant to Rule 13a-14(b) promulgated under the Securities Exchange Act of 1934, as amended, and Section 1350 of Chapter 63 of Title 18 of the United States Code. | | | |

| Exhibit No. | Filer | Description | Incorporated by Reference | | |
|-------------|-------|---|---------------------------|---------|-------------|
| | | | Form | Exhibit | Filing Date |
| *32.2 | (a) | Certification of Chief Financial Officer of Alliance Data Systems Corporation pursuant to Rule 13a-14(b) promulgated under the Securities Exchange Act of 1934, as amended, and Section 1350 of Chapter 63 of Title 18 of the United States Code. | | | |
| *101.INS | (a) | XBRL Instance Document | | | |
| *101.SCH | (a) | XBRL Taxonomy Extension Schema Document | | | |
| *101.CAL | (a) | XBRL Taxonomy Extension Calculation Linkbase Document | | | |
| *101.DEF | (a) | XBRL Taxonomy Extension Definition Linkbase Document | | | |
| *101.LAB | (a) | XBRL Taxonomy Extension Label Linkbase Document | | | |
| *101.PRE | (a) | XBRL Taxonomy Extension Presentation Linkbase Document | | | |

* Filed herewith

+ Management contract, compensatory plan or arrangement

(a) Alliance Data Systems Corporation

(b) WFN Credit Company

(c) World Financial Network Credit Card Master Trust

(d) World Financial Network Credit Card Master Note Trust

SIGNATURES

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

ALLIANCE DATA SYSTEMS CORPORATION

By: /s/ EDWARD J. HEFFERNAN
Edward J. Heffernan
President and Chief Executive Officer

Date: November 5, 2015

By: /s/ CHARLES L. HORN
Charles L. Horn
Executive Vice President and Chief Financial Officer

Date: November 5, 2015

**CERTIFICATION OF THE
CHIEF EXECUTIVE OFFICER
OF
ALLIANCE DATA SYSTEMS CORPORATION**

I, Edward J. Heffernan, certify that:

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

/s/ EDWARD J. HEFFERNAN

Edward J. Heffernan
Chief Executive Officer

Date: November 5, 2015

**CERTIFICATION OF THE
CHIEF FINANCIAL OFFICER
OF
ALLIANCE DATA SYSTEMS CORPORATION**

I, Charles L. Horn, certify that:

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

/s/ CHARLES L. HORN

Charles L. Horn
Chief Financial Officer

Date: November 5, 2015

**CERTIFICATION OF
CHIEF EXECUTIVE OFFICER
OF
ALLIANCE DATA SYSTEMS CORPORATION**

This certification is provided pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and accompanies the quarterly report on Form 10-Q for the quarter ended September 30, 2015 (the "Form 10-Q") of Alliance Data Systems Corporation (the "Registrant").

I, Edward J. Heffernan, certify that to the best of my knowledge:

(i) the Form 10-Q fully complies with the requirements of section 13(a) or section 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m(a) or 78o(d)); and

(ii) the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Registrant.

/s/ EDWARD J. HEFFERNAN
Edward J. Heffernan
Chief Executive Officer

Date: November 5, 2015

Subscribed and sworn to before me
this 5th day of November, 2015.

/s/ JANE BAEDKE
Name: Jane Baedke
Title: Notary Public

My commission expires:
October 23, 2016

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

**CERTIFICATION OF
CHIEF FINANCIAL OFFICER
OF
ALLIANCE DATA SYSTEMS CORPORATION**

This certification is provided pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and accompanies the quarterly report on Form 10-Q for the quarter ended September 30, 2015 (the "Form 10-Q") of Alliance Data Systems Corporation (the "Registrant").

I, Charles L. Horn, certify that to the best of my knowledge:

(i) the Form 10-Q fully complies with the requirements of section 13(a) or section 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m(a) or 78o(d)); and

(ii) the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Registrant.

/s/ CHARLES L. HORN
Charles L. Horn
Chief Financial Officer

Date: November 5, 2015

Subscribed and sworn to before me
this 5th day of November, 2015.

/s/ JANE BAEDKE
Name: Jane Baedke
Title: Notary Public

My commission expires:
October 23, 2016

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