

ITLA CAPITAL CORP
Form 10-K
March 15, 2004

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

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

For the Fiscal Year Ended December 31, 2003

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 0-26960

ITLA CAPITAL CORPORATION
(Exact Name of Registrant as Specified in its Charter)

Delaware
(State or Other Jurisdiction of Incorporation or Organization)

95-4596322
(I.R.S. Employer Identification No.)

888 Prospect Street, Suite 110, La Jolla, California
(Address of Principal Executive Offices)

92037
(Zip Code)

Registrant's Telephone Number, Including Area Code: **(858) 551-0511**

Securities Registered Pursuant to Section 12(b) of the Act:
None

Securities Registered Pursuant to Section 12(g) of the Act:
Common Stock, \$.01 Par Value
(Title of Class)

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

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

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

As of March 8, 2004, there were issued and outstanding 6,268,673 shares of the Registrant's Common Stock. The aggregate market value of the voting stock held by non-affiliates of the Registrant as of June 30, 2003, computed by reference to the closing price of such stock as of

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

June 30, 2003, was \$230.9 million. (The exclusion from such amount of the market value of the shares owned by any person shall not be deemed an admission by the Registrant that such person is an affiliate of the Registrant.)

TABLE OF CONTENTS

PART I

- Item 1. Business
- Item 2. Properties
- Item 3. Legal Proceedings
- Item 4. Submission of Matters to a Vote of Security Holders

PART II

- Item 5. Market for Registrant's Common Equity and Related Stockholder Matters
- Item 6. Selected Financial Data
- Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations
- Item 7A. Quantitative and Qualitative Disclosures About Market Risk
- Item 8. Financial Statements and Supplementary Data
- Item 9. Changes In and Disagreements With Accountants on Accounting and Financial Disclosure
- Item 9A. Controls and Procedures

PART III

- Item 10. Directors and Executive Officers of the Registrant
- Item 11. Executive Compensation
- Item 12. Security Ownership of Certain Beneficial Owners and Management
- Item 13. Certain Relationships and Related Transactions
- Item 14. Principal Accountant Fees and Services

PART IV

- Item 15. Exhibits, Financial Statement Schedules and Reports on Form 8-K

SIGNATURES

EXHIBIT 21

EXHIBIT 23.1

EXHIBIT 23.2

EXHIBIT 31.1

EXHIBIT 31.2

EXHIBIT 32

Table of Contents

ITLA CAPITAL CORPORATION
FORM 10-K
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2003

TABLE OF CONTENTS

		Page
PART I		
Item 1	Business	3
Item 2	Properties	15
Item 3	Legal Proceedings	15
Item 4	Submission of Matters to a Vote of Security Holders	15
PART II		
Item 5	Market for Registrant's Common Equity and Related Stockholder Matters	16
Item 6	Selected Financial Data	17
Item 7	Management's Discussion and Analysis of Financial Condition and Results of Operations	18
Item 7.A	Quantitative and Qualitative Disclosures About Market Risk	35
Item 8	Financial Statements and Supplementary Data	37
Item 9	Changes In and Disagreements With Accountants on Accounting and Financial Disclosure	64
Item 9.A	Controls and Procedures	64
PART III		
Item 10	Directors and Executive Officers of the Registrant	65
Item 11	Executive Compensation	67
Item 12	Security Ownership of Certain Beneficial Owners and Management	72
Item 13	Certain Relationships and Related Transactions	74
Item 14	Principal Accountant Fees and Services	74
PART IV		
Item 15	Exhibits, Financial Statement Schedules and Reports on Form 8-K	75
	Signatures	78
	Certifications	82

Forward-Looking Statements

Safe Harbor statement under the Private Securities Litigation Reform Act of 1995: This Form 10-K contains forward-looking statements that are subject to risks and uncertainties, including, but not limited to, changes in economic conditions in our market areas, changes in policies by regulatory agencies, the impact of competitive loan products, loan demand risks, the quality or composition of our loan or investment portfolios, fluctuations in interest rates and changes in the relative differences between short and long-term interest rates, levels of nonperforming assets and operating results, the impact of terrorist actions on our loan originations and loan repayments and other risks detailed from time to time in our filings with the Securities and Exchange Commission. We caution readers not to place undue reliance on forward-looking statements. We do not undertake and specifically disclaim any obligation to revise any forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date of such statements. These risks could cause our actual results for 2004 and beyond to differ materially from those expressed in any forward-looking statements by, or on behalf of, us.

As used throughout this report, the terms "we", "our", "ITLA Capital" or the "Company" refer to ITLA Capital Corporation and its consolidated subsidiaries.

Table of Contents

PART I

Item 1. Business

General

ITLA Capital Corporation is the largest financial services company headquartered in San Diego County, California with consolidated assets of \$1.8 billion, consolidated net loans of \$1.4 billion, consolidated deposits of \$1.1 billion and consolidated shareholders' equity of \$186.9 million as of December 31, 2003. We conduct and manage our business principally through our wholly-owned subsidiary, Imperial Capital Bank (the "Bank"), an institution with \$1.7 billion in assets, with six retail branches located in California, (Beverly Hills, Costa Mesa, Encino, Glendale, San Diego, and San Francisco), and one branch located in Carson City, Nevada. Additionally, the Bank has eight lending offices located in California (Del Mar, San Diego, Century City, Costa Mesa, Glendale, San Francisco, Santa Monica, and Walnut Creek) and five other lending offices, located in Atlanta, Georgia, Austin, Texas, Carson City, Nevada, Spokane, Washington, and Tempe, Arizona. On January 1, 2003, the Bank converted from a California industrial bank to a California-chartered commercial bank, and the Company became a bank holding company. The Bank has been in business for 29 years and was formally known as Imperial Thrift and Loan Association until its name change in January 2000. Our branch offices are primarily used for our deposit services and lending business. The Bank is primarily engaged in:

Originating real estate loans secured by income producing properties for retention in its loan portfolio;

Originating film finance loans, franchise loans, tax refund anticipation loans, private label small business revolving credit loans; and

Accepting customer deposits through the following products: certificates of deposits, money market, passbook and demand deposit accounts. Our deposit accounts are insured by the Federal Deposit Insurance Corporation ("FDIC") up to the legal limits.

During 2001 and 2000, the Bank was also engaged in the acquisition of pools of single family mortgages in the secondary market for investment purposes. On March 28, 2002, the Bank disposed of virtually all of its residential loan portfolio through the securitization of \$86.3 million of its performing single family mortgages and sale of \$17.6 million of the remaining single family mortgages in a whole loan sale.

During 2000, we acquired through our subsidiary, Imperial Capital Real Estate Investment Trust ("Imperial Capital REIT"), all of the equity and certain collateralized mortgage obligations ("CMOs") of the ICCMAC Multi-family and Commercial Trust 1999-1 (the "ICCMAC Trust"). On the date of acquisition, the ICCMAC Trust held assets of \$250.5 million as collateral for \$205.4 million of investment grade CMOs that had been sold to third party investors by the previous owner. At December 31, 2003 and 2002, real estate loans held in trust, net, for the CMOs totaled \$68.6 million and \$121.9 million and the CMOs outstanding balance was \$15.9 million and \$69.1 million, respectively.

During the first quarter of 2002, we completed our acquisition of Asahi Bank of California ("Asahi Bank"), a wholly-owned subsidiary of Asahi Bank Ltd - Japan ("ABLJ"), for approximately \$14.9 million in cash. On the date of acquisition, Asahi Bank had total assets of approximately \$50.0 million, including \$35.0 million of commercial real estate and business loans and \$15.0 million of cash and securities. Upon completion of the acquisition, Asahi Bank was merged into the Bank.

On October 25, 2002, we acquired the operating assets and the performing film finance loan portfolio of the Lewis Horwitz Organization ("LHO"), in an all cash transaction valued at approximately \$93.0 million. LHO is an internationally recognized lender to the independent film and television production industry. LHO is currently operating as a division of the Bank.

In November 2002, we entered into a strategic business relationship with various subsidiaries of Household International, Inc. ("Household"), a wholly-owned subsidiary of HSBC Holdings plc (NYSE: HBC) relating to certain tax refund products. In connection with this relationship, the Bank originates tax refund anticipation loans and sells Household a non-recourse participation interest representing substantially all of the outstanding loan balance. Under the agreement, Household supports the Bank's credit administration, compliance, treasury and accounting functions with a range of services relating to the administration of this program. Household also services the loans on behalf of the Bank. Substantially all of the tax refund lending volume is generated during the first quarter of the year. The tax refund agreement is for a four-year term, with substantial break-up fees to apply in the event that

Table of Contents

Household terminates the agreement during the first two years of the agreement. The Bank was affirmed by Household in November 2003, as its strategic banking partner for the 2004 tax season.

We also entered into an agreement in December 2002 with Household pursuant to which the Bank originates relatively small private label commercial revolving loans to small businesses. This agreement is for a two-year term. These loans are used primarily to fund purchases from major retailers. Pursuant to this agreement, the Bank sells Household a non-recourse participation interest representing substantially all of the outstanding loan balance.

We continuously evaluate business expansion opportunities, including acquisitions or joint ventures with companies that originate or purchase commercial and multi-family real estate loans as well as other types of secured commercial loans. In connection with this activity, we periodically have discussions with and receive financial information about other companies that may or may not lead to the acquisition of the company, a segment or division of that company, or a joint venture opportunity.

Our executive offices are located at 888 Prospect Street, Suite 110, La Jolla, California 92037 and our telephone number at that address is (858) 551-0511.

Lending Activities

General. During 2003, our core lending activities were as follows:

Originating and purchasing real estate loans, including construction loans, secured by income producing properties.

Originating and purchasing franchise and film finance loans.

Income Producing Property Loans. We originate and purchase real estate loans secured primarily by first trust deeds on income producing properties. Income property loan collateral consists primarily of the following types of properties:

- | | |
|---|--|
| Apartments | Mini-storage facilities |
| Retail centers | Mobile home parks |
| Small office and light industrial buildings | Other mixed use or special purpose commercial properties |
| Hotels | |

At December 31, 2003, the Bank had \$1.2 billion of income producing property loans outstanding, representing 89.9% of its total real estate loans and 77.7% of its gross loan portfolio. Most of the Bank's real estate borrowers are business owners, individual investors, investment partnerships or limited liability corporations. The income producing property lending that the Bank engages in typically involves larger loans to a single borrower and is generally viewed as exposing the lender to a greater risk of loss than one- to four-family residential lending. During 2002, we launched Imperial Capital Express, a real estate lending platform focusing on originating smaller balance income producing property loans.

Income producing property values are also generally subject to greater volatility than residential property values. The liquidation values of income producing properties may be adversely affected by risks generally incident to interests in real property, such as:

- | | |
|--|--|
| Changes or continued weakness in general or local economic conditions; | Changes in governmental rules, regulations and fiscal policies, including rent control ordinances, environmental legislation and taxation; |
| Changes or continued weakness in specific industry segments; | Increases in interest rates, real estate and personal property tax rates; and |
| Increases in other operating expenses (including energy costs); | Other factors beyond the control of the borrower or the lender. |
| Declines in real estate values; | |
| Declines in rental, room or occupancy rates in hotels, apartment complexes or commercial properties; | |

We originate real estate loans through six lending offices located in California (Costa Mesa, Del Mar, Glendale, San Diego, San Francisco, and Walnut Creek) and three offices outside of California, located in Atlanta, Georgia, Austin, Texas and Spokane, Washington. These offices are staffed by a total of thirty-six loan officers. Loan officers solicit mortgage loan brokers for loan applications that meet our underwriting criteria, and also accept applications directly from borrowers. A majority of the real estate loans funded by us are originated through mortgage loan brokers. Mortgage loan brokers act as intermediaries between us and the property owner in arranging real estate loans and earn a fee based upon the principal amount of each loan funded. Since a large portion

Table of Contents

of our marketing effort is through our loan officers' contacts with mortgage loan brokers, we do not incur significant expenses for advertising our lending services to the general public.

Income producing property loans are generally made in amounts up to 75% of the appraised value of the property; however, in certain instances, multifamily originations may be made at a loan to value ratio of 80%. Loans are generally made for terms up to ten years, with amortization periods up to 30 years. Depending on market conditions at the time the loan was originated, certain loan agreements may include prepayment penalties. Most real estate loans are subject to a quarterly adjustment of their interest rate based on one of several interest rate indexes.

The interest rates charged on real estate loans generally vary based on a number of factors, including the degree of credit risk, size and maturity of the loan, whether the loan has a fixed or a variable rate, and prevailing market rates for similar types of real estate loans. As of December 31, 2003, 64.1% of the Bank's real estate loan portfolio was indexed to the Six-Month London Interbank Offered Rate; 15.9% was indexed to the reference rate charged by Bank of America; 3% was indexed to the one-month London Interbank Offered Rate; 0.8% was indexed to the Federal Home Loan Bank (FHLB) 11th District Cost of Funds Index; 12.1% was fixed for an initial period and then adjustable; 0.5% was indexed to the United States Treasury security indexes; and the balance of 3.2% was fixed rate. Most of the Bank's variable rate real estate loans may not adjust downward below their initial rate, with increases generally limited to maximum adjustments of 2% per year up to 5% for the life of the loan. The inability of the Bank's real estate loans to adjust downward can contribute to increased income in periods of declining interest rates, and also assists the Bank in our efforts to limit the risks to earnings resulting from changes in interest rates, subject to the risk that borrowers may refinance these loans during periods of declining interest rates. At December 31, 2003, 88.8% of the Bank's variable rate and fixed/adjustable loan portfolio contained interest rate floors. The weighted-average minimum interest rate on this portfolio was 6.75%. At that date, 76.7% of the variable rate loans outstanding had a lifetime interest rate cap. The weighted-average lifetime interest rate cap on this portfolio was 11.92%.

In 2003, 2002, and 2001, the Bank purchased income producing real estate loans totaling \$46.8 million, \$83.6 million, and \$176.9 million, respectively. In its commercial real estate loan purchases, the Bank generally reserves the right to reject particular loans from a loan pool being purchased and does so for loans in a pool that do not meet its underwriting criteria.

Construction Loans. We originate construction loans for income producing properties, as well as for single-family residential tract construction. At December 31, 2003, the Bank had \$129.5 million of construction loans outstanding, representing 8.8% of its gross loans receivable. In addition to the lending risks previously discussed, construction loans also present risks associated with the accuracy of the initial estimate of the property's value upon completion compared to its actual value, the timely completion of construction activities for their allotted costs and the time needed to stabilize income properties. These risks can be affected by a variety of factors, including the oversight of the project, localized costs for labor and materials, and the weather.

Franchise Loans. In December 2002, the Bank expanded its franchise lending operations through the opening of the Imperial Franchise Finance, a franchise lending platform based in Tempe, Arizona. Prior to the opening of this new platform, under which we now originate, and continue to purchase, franchise loans, our franchise lending business primarily consisted of purchased franchise loans through our relationships with correspondent franchise loan originators. Franchise loans are loans to owners of businesses, both franchisors and franchisees, such as fast food restaurants or gasoline retailers that are affiliated with nationally or regionally recognized chains and brand names. Various combinations of land, building, business equipment and fixtures may secure these loans, or they may be a general obligation of the borrower based on a valuation of the borrower's business and debt service ability. These loans may be viewed as riskier than our real estate secured loans, as in each case, the primary source of repayment of a franchise loan is the cash flow of the business and not the underlying value of the collateral. In addition, in certain cases, the success of the borrower's business depends on the management talents and efforts of one or two persons or a small group of persons, and the death, disability or resignation of one or more of these persons could have a material adverse impact on the business. Many of these borrowers have smaller market shares than their competition, may be more vulnerable to economic downturns, often need additional capital to expand or compete and may experience substantial variations in operating results, any of which might impair the borrower's ability to repay a loan. As of December 31, 2003 and 2002, our franchise loan portfolio was \$102.1 million and \$54.7 million, respectively, which represented 6.7% and 4.1%, respectively, of the Bank's gross loan portfolio.

Film Finance Loans. We acquired LHO in October 2002 and are operating LHO as a division of the Bank. LHO is an internationally recognized commercial finance lender engaged in providing financing for independent motion picture and television production. Typically, LHO lends to independent producers of film and television on a senior secured basis, basing its credit decisions on the creditworthiness and reputation of distributors and sales agents who have contracted to distribute the films. LHO provides loans (with a typical term of 12 to 18 months) and letters of credit for the production of motion pictures and television shows or series that

Table of Contents

have a predictable market worldwide, and therefore, a predictable level of revenue arising from licensing of the distribution rights throughout the world.

LHO lends to independent producers of film and television, many of which are located in California. LHO also has borrowing clients outside of the United States. Independent producers tend to be those producers that do not have major studio distribution outlets for their product. Large film and television studios generally maintain their own distribution outlets and finance their projects with internally generated financing. In addition to funding production loans against a number of distribution contracts, LHO has a proprietary system related to valuation of selected unsold rights to permit financing of a portion of the production budget. Typically, this unsecured amount does not exceed 10% of the total loan. LHO's lending officers review the quality of the distributors and their contracts, the budget, the schedule of advances, and valuation of all distribution rights when considering a new lending opportunity. All LHO loans require the borrower to provide a completion bond that guarantees the completion of the film or the payoff of the outstanding balance of the loan in the event the film is not completed. After closing, each requested advance is approved by the bonding company on a weekly basis to ensure that LHO is not advancing ahead of an agreed-upon cash flow schedule. The loan documentation grants LHO the right to impose certain penalties on the borrower and exercise certain other rights, including replacing the sales agent, if sales are not consummated within the appropriate time. Loans are repaid principally from revenue received from distribution contracts. In many instances, the distribution contracts provide for multiple payments payable at certain milestones (such as execution of contract, commencement of principal photography or completion of principal photography). The maturity date of the loan is generally six to nine months after completion of the production. Delivery of the completed production is made to the various distributors only upon or after their minimum guarantees have been paid in full. To the extent a distributor fails to make payment upon completion of the film, or the predicted level of revenue is less than expected, the Bank may incur a loss.

LHO typically charges its customers an interest rate ranging from the prime rate to prime plus a margin (exclusive of loan fees) on the outstanding balance of the loan. Loan fees typically range from 1.00% to 2.50% with an additional fee up to 7.0% depending on the unsecured amount of the production budget being financed.

At December 31, 2003 and 2002, our film finance portfolio totaled \$98.6 million and \$119.3 million, respectively, representing 6.4% and 8.1% of our gross loan portfolio as of these dates. Of these amounts, approximately \$26.6 million and \$48.8 million, respectively, were issued to producers domiciled outside of the United States. These foreign loans were primarily issued to producers in Australia, Canada, and Germany. Approximately \$5.1 million and \$600,000 of interest income was earned during fiscal 2003 and 2002, respectively, in connection with these loans. At December 31, 2003, non-performing loans as a percentage of the LHO portfolio was 3.1%. There were no non-performing loans at December 31, 2002.

Loan Underwriting. Many of the Bank's loans are made to lower credit grade borrowers that have marginal credit histories or the property has other factors such as debt-to-income ratios or property location that prevent the borrower from obtaining a prime interest rate. We attempt to mitigate the risk associated with these loans by charging higher interest rates and through our loan approval and loan purchasing process. The Bank's loan underwriters are responsible for initial reviews of borrowers, collateral, loan terms, and prepare a written presentation on every loan application submitted to its loan committee, which is comprised of the following Bank officers:

Chairman, Chief Executive Officer, President	Managing Director/Deputy Chief Credit Officer-Administration
Vice Chairman and Chief Credit Officer	Managing Director/Deputy Chief Credit Officer-Production
Senior Managing Director/Chief Banking Officer	Deputy Managing Director/Business Credit
Managing Director/Chief Lending Officer	First Vice President/Manager Loan Underwriting

The underwriting standards for loans secured by income producing real estate properties consider the borrower's financial resources and ability to repay and the amount and stability of cash flow, if any, from the underlying collateral, to be comparable in importance to the loan-to-value ratio as a repayment source.

All real estate secured loans over \$2.0 million must be submitted to the loan committee for approval. At least one loan committee member or designee must personally conduct on-site inspections of any property involved in connection with a real estate loan recommendation of \$1.0 million or more. Loans up to \$750,000 may be approved by any loan committee member. Loans of \$750,000 to \$1.5 million require approval by any two members of the Bank's loan committee, while loans in excess of \$1.5 million require approval of three loan committee members. Additionally, loans over \$2.0 million must be approved by the Managing Director/Deputy Chief Credit Officer-Administration; loans over \$3.0 million require the additional signature of the Vice Chairman and Chief Credit Officer; and individual loans over \$5.0 million, loans resulting in an aggregate borrowing relationship to one borrower in excess of \$7.5 million, and all purchased loan pools must be approved by the executive committee of the Bank's board of directors.

Table of Contents

All franchise and film finance loans must be submitted to the loan committee for approval regardless of the amount of the loan request. Loan amounts up to \$2.0 million require the approval of three loan committee members. Loans over \$2.0 million must be approved by the First Vice President of Business Lending Operations and loans over \$3.0 million must be approved by the Vice Chairman and Chief Credit Officer.

Our loans are originated on both a non-recourse and full recourse basis and we generally seek to obtain personal guarantees from the principals of borrowers which are single asset or limited liability entities (such as partnerships, corporations or trusts).

The maximum size of a single loan made by the Bank is limited by California law to 25% of the Bank's equity capital. At December 31, 2003, that limit was approximately \$54.5 million. The Bank's largest combined credit extension to related borrowers was \$25.7 million at December 31, 2003. At December 31, 2003, the Bank had a total of 74 extensions of credit, with a combined outstanding principal balance of \$660.8 million, that were over \$5.0 million to a single borrower or related borrowers. All combined extensions of credit over \$5.0 million were performing in accordance with their repayment terms. At December 31, 2003, the Bank had 1,502 secured real estate loans outstanding, with an average balance per loan of approximately \$837,000.

Servicing and Collections. Real estate loans, construction loans, film finance and internally originated franchise loans held by the Bank are serviced by the Bank's loan servicing department, which is designed to provide prompt customer service, and accurate and timely information for account follow-up, financial reporting and management review. Servicing of substantially all of the purchased franchise loan portfolio and loans held in the ICCMAC Trust is performed by third party servicers. The Bank monitors its loans to ensure that projects are performing as underwritten. This monitoring allows the Bank to take a proactive approach to addressing projects that do not perform as planned. When payments are not received by their contractual due date, collection efforts begin on the fifth day of delinquency with a telephone contact, and proceed to written notices that progress from reminders of the borrower's payment obligation to an advice that a notice of default may be forthcoming. Accounts delinquent for more than 30 days are generally transferred to the Bank's asset management department which, following a review of the account and management approval, implements a collection or restructure plan, or a disposition strategy, and evaluates any potential loss exposure on the asset.

Competition. Our competition in originating real estate, construction, franchise and film finance loans is principally from community banks, savings and loan associations, industrial banks, real estate financing conduits, specialty finance companies, small insurance companies, and larger banks. Many of these entities enjoy competitive advantages over us relative to a potential borrower in terms of a prior business relationship, wider geographic presence or more accessible branch office locations, the ability to offer additional services or more favorable pricing alternatives, or a lower cost of funds structure. We attempt to offset the potential effect of these factors by providing borrowers with greater individual attention and a more flexible and time-sensitive underwriting, approval and funding process than they might obtain elsewhere.

Household Strategic Alliance

Tax Refund Lending. In November 2002, we entered into a strategic business relationship with various subsidiaries of Household relating to certain tax refund anticipation loans. In connection with this relationship, the Bank originates tax refund anticipation loans, and sells to Household a non-recourse participation interest representing substantially all of the outstanding loan balance. The tax refund agreement with Household is for a four-year term, with substantial break-up fees to apply in the event that Household terminates the agreement during the initial two-year period. The Bank was affirmed by Household in November 2003, as its strategic banking partner for the 2004 tax season. Household supports our credit administration, compliance, treasury and accounting functions with a range of services relating to the administration of this lending program. The Bank would not originate these loans without the involvement of Household or a similar business partner.

Pursuant to our agreement with Household, the Bank offers tax refund anticipation loans (RALs) to taxpayers who have filed their returns electronically with the IRS and do not want to wait for the IRS to send them their refund check. For this product, a taxpayer requests a loan through a tax preparer, with the anticipated tax refund as the source of repayment. The taxpayer's application is then subjected to an automated credit review process. If the application passes this review, the Bank advances to the taxpayer the amount of the refund due on the taxpayer's return up to specified amounts based on certain criteria, less a pre-paid finance charge and certain other fees. Each taxpayer signs an agreement permitting the IRS to send their refund directly to the Bank instead of to the taxpayer. The refund received from the IRS is used to pay off the loan. Any amount due the taxpayer above the amount of the RAL is then sent to the taxpayer. The Bank also provides refund transfers to customers who do not want or do not qualify for loans. The transfer product facilitates the receipt of the refund by the customer by authorizing the customer's tax preparer to print a check for the customer after the refund has been received by the Bank from the IRS (RACs). Because of the mid-April tax-filing deadline, almost all of the loans and transfers are made and repaid during the first quarter of the year. The Bank's revenue, under the program, consists

Table of Contents

of RAL and RAC transaction fees and the earnings stream from RALs originated under the program to the extent of its retained interest in such RALs.

There is a higher credit risk associated with refund loans than with other types of loans because (1) the Bank does not have personal contact with the customers of this product; and (2) the customers conduct no business with the Bank other than this once a year transaction. Much of this risk is eliminated due to the immediate sale by the Bank to Household, of a participation interest representing virtually all of the RAL outstanding balance.

Because these programs relate to the filing of income tax returns, activity is concentrated in the first quarter of each year. This causes first quarter net income to become a greater percentage of each year's net income. This seasonality impacts a number of performance ratios, including return on assets (ROA), return on equity (ROE) and the operating efficiency ratio. These impacts are apparent in both the first quarter of 2003 and the year-to-date ratios in subsequent quarters. At December 31, 2003 and 2002, there were no RAL loans outstanding.

Private Label Commercial Revolving Credit Loans. We also entered into an agreement in December 2002 with Household pursuant to which the Bank originates private label small commercial revolving loans to small businesses. This agreement is for a two-year term. These loans are used primarily for purchases from major retailers. Pursuant to this agreement, the Bank sells Household a non-recourse participation interest representing substantially all of the outstanding loan balance. The Bank participates in the earnings stream from the loans originated under the program to the extent of its retained interest in such loans. At December 31, 2003 and 2002, our retained interest in commercial revolving credit loans was \$5.8 million and \$4.2 million, respectively.

Imperial Capital Real Estate Investment Trust

During 2000, we acquired all of the equity and certain CMOs of the ICCMAC Trust through our real estate investment trust subsidiary, Imperial Capital REIT. At December 31, 2003, the ICCMAC Trust held real estate loans of \$68.6 million, comprised of approximately 67.0% and 33.0% of multifamily and commercial loans, respectively, with over 45.9% of the loans secured by property located in California. Approximately two-thirds of the loans are adjustable rate mortgages. At December 31, 2003, the ICCMAC Trust's real estate loans were held as collateral for \$15.9 million of investment grade CMOs sold to third party investors. The cash flow from the ICCMAC Trust's loan pool pays principal and interest on the CMOs, and also provides cash flow on a monthly basis to ITLA Capital. ITLA Capital recorded \$3.5 million of pre-tax income from its investment in the ICCMAC Trust during the year ended December 31, 2003.

Servicing of the ICCMAC Trust loans is performed by Orix Capital Markets, LLC (Orix), a Delaware limited liability company. Under the servicing agreement, Orix is required to service and administer the commercial mortgage loans held in trust solely for the benefit of the holders of the CMOs in accordance with the terms of the servicing agreement and the commercial mortgage loans.

Orix is required to perform other customary functions of a servicer of comparable loans, including monitoring insurance coverage; maintaining escrow or impoundment accounts of borrowers for payment of taxes, insurance and other items required to be paid pursuant to the loan agreement; processing assumptions or substitutions in those cases where the loan servicer has determined not to enforce any applicable due-on-sale clause; demanding that the borrower cure delinquencies; inspecting and managing commercial mortgaged properties under certain circumstances; and maintaining records relating to the commercial mortgage loans.

Nonperforming Assets and Other Loans of Concern

At December 31, 2003, nonperforming assets totaled \$15.6 million or 0.86% of total assets. Nonperforming assets consisted of \$8.5 million of nonaccrual loans and \$7.1 million of other real estate owned. Two of our nonperforming loans had an outstanding balance greater than \$1.0 million. For additional information regarding nonperforming assets see Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations-Credit Risk Elements .

The following is a brief discussion of the non-accrual loans where the remaining principal balance of the loan at December 31, 2003, exceeded \$1.0 million.

Loan Secured by Hotel - Arizona. This loan was originated in May 1997 with an initial commitment of \$2.2 million. The loan is secured by a 90-unit motel and the outstanding balance at December 31, 2003 was \$1.4 million. The cash flows generated by the property have been insufficient to service the debt. A partner of the borrower, a partnership, has agreed to loan the borrower sufficient funds to cure the current delinquencies.

Table of Contents

Loan Secured by Film Rights. This loan was purchased as a part of the LHO acquisition in 2002. The loan is secured by domestic and international film rights and the outstanding balance at December 31, 2003 was \$1.6 million. The loan has been cross collateralized with excess cash flows expected to be received by the borrower from film rights on separate projects. These excess cash flows are expected to be sufficient to pay off this loan.

As of December 31, 2003, we had loans with an aggregate outstanding balance of \$31.3 million with respect to which known information concerning possible credit problems with the borrowers or the cash flows of the properties securing the respective loans has caused management to be concerned about the ability of the borrowers to comply with present loan repayment terms, which may result in the future inclusion of such loans in the non-accrual loan category. All of these loans are classified as substandard pursuant to the regulatory guidelines discussed below. The following is a brief discussion of our other loans of concern where the remaining principal balance of the loan at December 31, 2003 exceeded \$2.0 million.

Loan Secured by Hotel - Arizona. This loan was originated in May 1997 with an initial commitment of \$4.0 million. The loan is secured by a 99-unit motel and the outstanding balance at December 31, 2003 was \$2.7 million. The cash flows generated by the property have been historically insufficient to service the debt, however, the most recent year-to-date operating financial information shows marked improvement in occupancy and cash flows, with a debt coverage ratio more than sufficient to service the debt. We continue to monitor the borrowers' efforts to improve the cash flow of this hotel.

Loan Secured by Hotel - California. This loan was originated in June 2001 with an initial commitment of \$3.3 million. The loan is secured by a 93-room hotel and the outstanding balance at December 31, 2003 was \$3.1 million. The property has suffered from declining occupancy. The borrower continues to pay in accordance with the loan repayment terms. We continue to monitor the borrowers' efforts to improve cash flow of this hotel through improvements to the property.

Loan Secured by Hotel - California. This loan was originated in December 1998 with an initial commitment of \$2.6 million. The loan is secured by a 61-room hotel and the outstanding balance at December 31, 2003 was \$2.5 million. The borrower continues to pay in accordance with the loan repayment terms.

Loan Secured by Hotel - California. This loan was originated in April 1998 with an initial commitment of \$3.2 million. The loan is secured by a 204-room hotel and the outstanding balance at December 31, 2003 was \$2.6 million. The cash flows generated by the property have been insufficient to service the debt and property taxes are delinquent. The borrower has appealed the property tax assessment and is expected to bring delinquent taxes current in early 2004. We continue to monitor the borrower's efforts to improve the cash flow of this hotel.

Loan Secured by Single Resident Occupancy - California. This loan was originated in May 2002 with an initial commitment of \$2.3 million. The loan is secured by a 96-unit single resident occupancy and the outstanding balance at December 31, 2003 was \$2.0 million. The property is 50% occupied. The borrower is currently in the process of obtaining financing to convert the property into a limited service hotel.

Loan Secured by Retail Center - Arkansas. This loan was originated in October 1998 with an initial commitment of \$5.3 million. The loan is secured by the subject retail center and the outstanding balance at December 31, 2003 was \$4.8 million. The property is 56% occupied and the borrower is paying as agreed under the terms of its forbearance agreement. The property is listed for sale and a letter of intent to purchase the property has been received. Closing of the sale is expected to be completed by the expiration of the forbearance period.

Loan Secured by Franchises - Tennessee. This loan was originated in February 2001 with an initial commitment of \$3.5 million. The loan is secured by four franchise restaurants and the outstanding balance at December 31, 2003 was \$3.3 million. The restaurants have been suffering from declining sales resulting in the borrower not being in compliance with the covenants contained in its loan agreement. The franchisor is assisting the borrower through a consultant to develop a plan to restore sales to appropriate levels. We continue to monitor the sales growth of these restaurants.

Loan Secured by Office Building - California. This loan was originated in May 2003 with an initial commitment of \$3.7 million. The borrower has struggled to replace a large tenant that vacated in mid-2003. As of December 31, 2003, the borrower had been late with payments and was past due on taxes and insurance related to the property. The note was sold in January 2004 and we received full payment.

At December 31, 2003, the other real estate owned portfolio consisted of four properties located throughout the United States. The largest property had a net book value of \$4.8 million at December 31, 2003.

Table of Contents

Classified Assets

Management uses a loan classification system consistent with the classification system used by bank regulatory agencies to help it evaluate the risks inherent in its real estate loan portfolio. Loans are identified as pass, substandard, doubtful or loss based upon consideration of all sources of repayment, underlying collateral values, current and anticipated economic conditions, trends and uncertainties, and historical experience. Pass loans are further divided into four additional sub-categories, based on the borrower's financial strength and ability to service the debt and/or the value and debt service coverage of the underlying collateral. Underlying collateral values for real estate dependent loans are supported by property appraisals or evaluations. We review our loan classifications on at least a quarterly basis. At December 31, 2003, we classified \$39.8 million of loans as substandard, none as doubtful and none as loss of which, \$8.5 million of these classified loans were included in the nonperforming assets table in Item 7. Management's Discussion and Analysis of Results of Financial Condition and Operations - Credit Risk Elements, and the balance was included in the \$31.3 million of other loans of concern, discussed above.

Funding Sources

The primary source of funding for the Bank's lending operations and investments are deposits. The Bank's deposits are federally insured by the FDIC to the maximum extent permitted by law. Approximately 82.2% of the Bank's deposits are term deposits that pay fixed rates of interest for periods ranging from 90 days to five years, 13.6% of the Bank's deposits are variable rate passbook accounts and variable rate money market accounts with limited checking features, and 4.2% are customer demand deposit accounts.

In connection with the Bank's charter conversion in 2003, we expanded our line of banking products and services offered to our customers. The new products and services consist of commercial banking products and services, including consumer and business checking accounts. The Bank's retail checking account balance was \$47.6 million at December 31, 2003. As we continue to expand and grow our retail deposit base, we anticipate that the Bank's dependence on interest rate sensitive certificates of deposit as a funding source will slowly diminish; however, in 2003, the Bank's deposit strategy continued to rely upon offering deposit rates significantly above those customarily offered by other financial institutions in its market. The Bank has generally accumulated deposits by relying on renewals of term accounts by existing depositors, participating in deposit rate surveys which promote the rates offered by the Bank on its deposit products, and periodically advertising in various local market newspapers and other media. Management believes that its deposits are a reliable funding source and that the cost of funds resulting from the Bank's deposit gathering strategy is comparable to those of other banks pursuing a similar strategy. However, because the Bank competes for deposits primarily on the basis of rates, the Bank could experience difficulties in attracting deposits if it could not continue to offer deposit rates at levels above those of other financial institutions. Management also believes that any efforts to significantly increase the size of its deposit base may require greater marketing efforts and/or increases in deposit rates. At December 31, 2003, the Bank had \$126.8 million of brokered deposits.

For information concerning overall deposits outstanding during the periods indicated and the rates paid thereon, see Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations - Net Interest Income.

The Bank has also used advances from the FHLB of San Francisco as a funding source. FHLB advances are collateralized by pledges of qualifying cash equivalents, investment securities, mortgage-backed securities and whole loan collateral. At December 31, 2003, FHLB advances outstanding totaled \$362.1 million, and the remaining available borrowing capacity, based on the loans and securities pledged as collateral, totaled \$161.0 million, net of the \$8.5 million of additional FHLB Stock that we would be required to purchase to support the additional borrowings. Additionally, the Bank also has uncommitted, unsecured lines of credit with other banks renewable daily in the amount of \$30.0 million. In connection with our tax refund lending business, ITLA Capital has two \$25.0 million revolving credit facilities with an unaffiliated bank. These credit facilities mature on March 31, 2004 and January 1, 2005, respectively. See Item 8. Financial Statements and Supplementary Data - Notes to Consolidated Financial Statements - Notes 8, 9, 11, and 22.

Regulation

On January 1, 2003, the Bank converted from a California industrial bank to a California-chartered commercial bank, and the Company became a bank holding company. As a result, the Company is now regulated by the Board of Governors of the Federal Reserve System (the Federal Reserve Board). The Bank continues to be regulated by the California Department of Financial Institutions (the DFI) and the Federal Deposit Insurance Corporation (the FDIC). Due to legislation which became effective in October 2000, California industrial banks are now generally subject to the same California banking laws as California commercial banks. Accordingly, the regulatory oversight to which the Bank is now subject as a commercial bank is not significantly different from the regulatory oversight to which it was subject as an industrial bank.

Table of Contents

Holding Company Regulation

Bank holding companies are subject to comprehensive regulation by the Federal Reserve Board under the Bank Holding Company Act of 1956, and the regulations of the Federal Reserve Board. As a bank holding company, the Company is required to file reports with the Federal Reserve Board and such additional information as the Federal Reserve Board may require, and the Company and its non-bank subsidiaries are subject to examination by the Federal Reserve Board. The Federal Reserve Board also has extensive enforcement authority over bank holding companies, including, among other things, the ability to assess civil money penalties, to issue cease and desist or removal orders and to require that a bank holding company divest subsidiaries, including its bank subsidiaries. In general, enforcement actions may be initiated for violations of law and regulation as well as unsafe or unsound practices.

Under Federal Reserve Board policy, a bank holding company must serve as a source of strength for its subsidiary banks. Under this policy, the Federal Reserve Board may require, and has required in the past, bank holding companies to contribute additional capital to undercapitalized subsidiary banks.

Under the Bank Holding Company Act of 1956, a bank holding company must obtain Federal Reserve Board approval before, among other matters:

acquiring, directly or indirectly, ownership or control of any voting shares of another bank or bank holding company if, after the acquisition, it would own or control more than 5% of these shares (unless it already owns or controls a majority of these shares);

acquiring all or substantially all of the assets of another bank or bank holding company; or

merging or consolidating with another bank holding company.

This statute also prohibits a bank holding company, with certain exceptions, from acquiring direct or indirect ownership or control of more than 5% of the voting shares of any company which is not a bank or bank holding company, or from engaging directly or indirectly in activities other than those of banking, managing or controlling banks, or providing services for its subsidiaries. The principal exceptions to these prohibitions involve certain non-bank activities which have been identified as activities closely related to the business of banking or managing or controlling banks.

Dividends. The Federal Reserve Board has issued a policy statement on the payment of cash dividends by bank holding companies, which expresses the Federal Reserve Board's view that a bank holding company should pay cash dividends only to the extent that its net income for the past year is sufficient to cover both the cash dividends and a rate of earnings retention that is consistent with the bank holding company's capital needs, asset quality and overall financial condition. Furthermore, under its source of strength doctrine, the Federal Reserve Board expects a bank holding company to serve as a source of financial strength for its bank subsidiaries, which could limit the ability of a holding company to pay dividends if a bank subsidiary did not have sufficient capital.

Repurchase or Redemption of Equity Securities. A bank holding company is required to give the Federal Reserve Board prior written notice of any purchase or redemption of its outstanding equity securities if the gross consideration for the purchase or redemption, when combined with the net consideration paid for all such purchases or redemptions during the preceding 12 months, is equal to 10% or more of its consolidated net worth. The Federal Reserve Board may disapprove such a purchase or redemption if it determines that the proposal would constitute an unsafe or unsound practice or would violate any law, regulation, Federal Reserve Board order, or any condition imposed by, or written agreement with, the Federal Reserve Board. This notification requirement does not apply to any company that meets the well-capitalized standard for bank holding companies, has a safety and soundness examination rating of at least a 2 and is not subject to any unresolved supervisory issues.

Regulatory Capital Requirements. The Federal Reserve has established risk-based measures and a leverage measure of capital adequacy for bank holding companies. The Company was not subject to any minimum capital requirements prior to becoming a bank holding company.

The risk-based capital standards are designed to make regulatory capital requirements more sensitive to differences in risk profiles among banks and bank holding companies, to account for off-balance-sheet exposure, and to minimize disincentives for holding liquid assets. Assets and off-balance-sheet items, such as letters of credit and unfunded loan commitments, are assigned to broad risk categories, each with appropriate risk weights. The resulting capital ratios represent capital as a percentage of total risk-weighted assets and off-balance-sheet items.

Table of Contents

The minimum ratio of total capital to risk-weighted assets is 8.0%. Total capital consists of two components, Tier 1 capital and Tier 2 capital. Tier 1 capital generally consists of common shareholders' equity, including retained earnings, noncumulative perpetual preferred stock, certain trust preferred securities and minority interest in equity accounts of fully consolidated subsidiaries, less goodwill and other specified intangible assets. Tier 1 capital must equal at least 4.0% of risk-weighted assets. Tier 2 capital generally consists of subordinated debt and other hybrid capital instruments, other preferred stock, a limited amount of loan loss reserves and a limited amount of unrealized holding gains on equity securities. The total amount of Tier 2 capital is limited to 100% of Tier 1 capital. At December 31, 2003, our ratio of total capital to risk-weighted assets was 18.2% and our ratio of Tier 1 capital to risk-weighted assets was 15.6%.

In addition, the Federal Reserve has established minimum leverage ratio guidelines for bank holding companies. These guidelines provide for a minimum ratio of Tier 1 capital to average assets, less goodwill and other specified intangible assets, of 3.0% for bank holding companies that meet specified criteria, including having the highest regulatory rating and implementing the Federal Reserve's risk-based capital measure for market risk. All other bank holding companies generally are required to maintain a leverage ratio of at least 4.0%. At December 31, 2003, the Company's required Tier 1 capital ratio was 4.0% and our actual Tier 1 capital was 15.3%.

The Company currently is deemed well capitalized under the Federal Reserve Board capital requirements. To be well capitalized, a bank holding company must have a ratio of total capital to risk weighted assets of at least 10% and a ratio of Tier 1 capital to risk weighted assets of at least 6.0%.

Failure to meet capital guidelines could subject a bank or bank holding company to a variety of enforcement remedies, including issuance of a capital directive, the termination of deposit insurance by the FDIC, a prohibition on accepting brokered deposits, and other restrictions on its business. As described below, significant additional restrictions can be imposed on FDIC-insured depository institutions that fail to meet applicable capital requirements.

Bank Regulation California Law

The regulations of the DFI govern most aspects of the Bank's businesses and operations, including, but not limited to, the scope of its business, investments, the nature and amount of any collateral for loans, the issuance of securities, the payment of dividends, bank expansion and bank activities. The DFI's supervision of the Bank includes comprehensive reviews of all aspects of the Bank's business and condition, and the DFI possesses broad remedial enforcement authority to influence the Bank's operations, both formally and informally.

Bank Regulation Federal Law

Because our deposits are insured by the Bank Insurance Fund of the FDIC, the FDIC, in addition to the DFI, also broadly regulates the Bank. As an insurer of deposits, the FDIC issues regulations, conducts examinations, requires the filing of reports, and generally supervises the operations of institutions to which it provides deposit insurance. The FDIC is also the federal agency charged with regulating state-chartered banks that are not members of the Federal Reserve System, such as the Bank. Insured depository institutions, and their institution-affiliated parties, may be subject to potential enforcement actions by the FDIC and the DFI for unsafe or unsound practices in conducting their businesses or for violations of any law, rule, regulation or any condition imposed in writing by the agency or any written agreement with the agency. Management is not aware of any pending or threatened enforcement actions against the Bank.

Regulatory Capital Requirements. Federally-insured, state-chartered banks such as the Bank, are required to maintain minimum levels of regulatory capital as specified in the FDIC's capital maintenance regulations. The FDIC also is authorized to impose capital requirements in excess of these standards on individual banks on a case-by-case basis.

The Bank is required to comply with three separate minimum capital requirements: a tier 1 capital ratio and two risk-based capital requirements. Tier 1 capital generally includes common shareholders' equity, including retained earnings, qualifying noncumulative perpetual preferred stock and any related surplus, and minority interests in the equity accounts of fully consolidated subsidiaries, less intangible assets, other than properly valued purchased mortgage servicing rights up to certain specified limits and less net deferred tax assets in excess of certain specified limits.

Tier 1 Capital Ratio. FDIC regulations establish a minimum 3.0% ratio of Tier 1 capital to total average assets for the most highly-rated state-chartered, FDIC-supervised banks. All other FDIC supervised banks must maintain at least a 4.0% tier 1 capital ratio. At December 31, 2003, the Bank's required tier 1 capital ratio was 4.0% and its actual tier 1 capital ratio was 14.2%.

Table of Contents

Risk-Based Capital Requirements. The risk-based capital requirements generally require the Bank to maintain a ratio of tier 1 capital to risk-weighted assets of at least 4.0% and a ratio of total risk-based capital to risk-weighted assets of at least 8.0%. To calculate the amount of capital required, assets are placed in one of four categories and given a percentage weight (0%, 20%, 50% or 100%) based on the relative risk of the category. For example, United States Treasury Bills and Ginnie Mae securities are placed in the 0% risk category. Fannie Mae and Freddie Mac securities are placed in the 20% risk category, loans secured by one-to four-family residential properties and certain privately-issued mortgage-backed securities are generally placed in the 50% risk category, and commercial and consumer loans and other assets are generally placed in the 100% risk category. In addition, certain off-balance-sheet items are converted to balance sheet credit equivalent amounts and each amount is then assigned to one of the four categories.

For purposes of the risk-based capital requirements, total capital means tier 1 capital plus supplementary or tier 2 capital, so long as the amount of supplementary or tier 2 capital that is used to satisfy the requirement does not exceed the amount of tier 1 capital. Tier 2 capital includes cumulative and certain other perpetual preferred stock, mandatory convertible subordinated debt and perpetual subordinated debt, mandatory redeemable preferred stock, intermediate-term preferred stock, mandatory convertible subordinated debt and subordinated debt, the allowance for loan losses up to a maximum of 1.25% of risk-weighted assets and a limited amount of unrealized holding gains on securities. At December 31, 2003 the Bank's tier 1 risk-based and total capital ratios were 14.3% and 15.6%, respectively.

The federal banking agencies have adopted regulations specifying that the agencies will include, in their evaluation of a bank's capital adequacy, an assessment of the exposure to declines in the economic value of the bank's capital due to changes in interest rates. The FDIC and the other federal banking agencies have also promulgated final amendments to their respective risk-based capital requirements which identify concentration of credit risk and certain risks arising from nontraditional activities, and the management of such risk, as important factors to consider in assessing an institution's overall capital adequacy. The FDIC may require higher minimum capital ratios based on certain circumstances, including where the institution has significant risks from concentration of credit or certain risks arising from nontraditional activities.

Prompt Corrective Action Requirements. The FDIC has implemented a system requiring regulatory sanctions against state-chartered banks (which, for this purpose, includes the Bank) that are not adequately capitalized, with the sanctions growing more severe the lower the institution's capital. The FDIC has established specific capital ratios for five separate capital categories: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized.

An institution is treated as well capitalized if its total risk based capital ratio is 10.0% or more, its tier 1 risk-based ratio is 6.0% or more, its tier 1 capital ratio is 5.0% or greater, and it is not subject to any order or directive by the FDIC to meet a specific capital level. The Bank exceeded these requirements at December 31, 2003.

The FDIC is authorized and, under certain circumstances, required to take certain actions against institutions that fail to meet their capital requirements. The FDIC is generally required to take action to restrict the activities of an undercapitalized institution. Any such institution must submit a capital restoration plan and, until such plan is approved by the FDIC, may not increase its assets, acquire another institution, establish a branch or engage in any new activities, and generally may not make capital distributions. The capital restoration plan must include a limited guaranty by the institution's holding company.

In addition, the FDIC must appoint a receiver or conservator for an institution, with certain limited exceptions, within 90 days after it becomes critically undercapitalized. Any undercapitalized institution is also subject to the general enforcement authority of the FDIC, including the appointment of a conservator or a receiver.

The FDIC is also generally authorized to reclassify an institution into a lower capital category and impose the restrictions applicable to such category if the institution is engaged in unsafe or unsound practices or is in an unsafe or unsound condition.

Community Reinvestment Act and Fair Lending Requirements. The Bank is subject to certain fair lending requirements and reporting obligations involving lending operations and Community Reinvestment Act activities. Federal banking agencies are required to evaluate the record of financial institutions in meeting the credit needs of their local communities, including low and moderate income neighborhoods. In addition to substantial penalties and corrective measures that may be required for a violation of certain fair lending laws, the federal banking agencies take compliance with such laws into account when regulating and supervising other activities such as mergers and acquisitions. In its most recent examination, the FDIC rated the Bank satisfactory in complying with its Community Reinvestment Act obligations.

Fiscal and Monetary Policies. Our business and earnings are affected significantly by the fiscal and monetary policies of the federal government and its agencies. We are particularly affected by the policies of the Federal Reserve Board, which regulates the

Table of Contents

supply of money and credit in the United States. Among the instruments of monetary policy available to the Federal Reserve Board are (a) conducting open market operations in United States government securities; (b) changing the discount rates of borrowings of depository institutions, (c) imposing or changing reserve requirements against depository institutions' deposits, and (d) imposing or changing reserve requirements against certain borrowings by banks and their affiliates. These methods are used in varying degrees and combinations to directly affect the availability of bank loans and deposits, as well as the interest rates charged on loans and paid on deposits. The policies of the Federal Reserve Board may have a material effect on the Company's business, results of operations and financial condition.

Privacy Provisions of the Gramm-Leach-Bliley Act. Federal banking regulators, as required under the Gramm-Leach-Bliley Act (the "GLB Act"), have adopted rules limiting the ability of banks and other financial institutions to disclose nonpublic information about consumers to nonaffiliated third parties. The rules require disclosure of privacy policies to consumers and, in some circumstances, allow consumers to prevent disclosure of certain personal information to nonaffiliated third parties. The privacy provisions of the GLB Act will affect how consumer information is transmitted through diversified financial service companies and conveyed to outside vendors. The GLB Act permits states to enact their own privacy rules which may be stricter than those under the GLB Act. We cannot predict at this time what terms will be considered in any proposed California privacy legislation, whether any such proposed legislation will be enacted and if so, when such legislation may become effective. Therefore, it is not possible at this time to assess fully the impact of the privacy provisions on our business, results of operations or financial condition.

Future Legislation. Various legislation, including proposals to change substantially the financial institution regulatory system, is from time to time introduced in Congress. This legislation may change banking statutes and our operating environment in substantial and unpredictable ways. If enacted, this legislation could increase or decrease the cost of doing business, limit or expand permissible activities or affect the competitive balance among banks, savings associations, credit unions, and other financial institutions. We cannot predict whether any of this potential legislation will be enacted and, if enacted, the effect that it, or any implementing regulations, would have on our business, results of operations or financial condition.

Employees

As of December 31, 2003, we had 230 employees. Management believes that its relations with employees are satisfactory. We are not subject to any collective bargaining agreements.

Segment Reporting

Financial and other information regarding our operating segments is contained in Note 20 to our audited consolidated financial statements included in Item 8 of this report.

Internet Website

We maintain a website with the address www.itlacapital.com. The information contained on our website is not included as a part of, or incorporated by reference into, this Annual Report on Form 10-K. Other than an investor's own Internet access charges, we make available free of charge through our website our Annual Report on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, and amendments to these reports, as soon as reasonably practicable after we have electronically filed such material with, or furnished such material to, the Securities and Exchange Commission.

Table of Contents**Item 2. Properties**

ITLA Capital leases approximately 82,462 square feet of office space for its operations as shown below.

Locations	Office Uses	Square Footage	Year Current Lease Term Expires
La Jolla, CA	Corporate Headquarters	17,419	2008
La Jolla, CA	Administrative and Marketing	2,325	2006
Glendale, CA	Loan Administration/Asset Management/Bank Branch	6,257	2006
Glendale, CA	Loan Operations Division/Real Estate Lending	8,932	2005
Del Mar, CA	Real Estate Lending	2,847	2004
Costa Mesa, CA	Bank Branch/Real Estate Lending	3,609	2006
San Francisco, CA	Bank Branch/Real Estate Lending	5,005	2007
Beverly Hills, CA	Bank Branch	2,218	2005
Encino, CA	Bank Branch/Information Systems Operations	5,298	2004
San Diego, CA	Bank Branch	3,046	2010
Santa Monica, CA	Imperial Capital Express Loan Operations/Real Estate Lending	4,991	2004
Walnut Creek, CA	Imperial Capital Express Real Estate Lending	2,220	2007
Century City, CA	Lewis Horwitz Organization	7,003	2008
Encino, CA	Operation Support	3,170	2004
Carson City, NV	Bank Branch/RAL and Private Label Commercial Revolving Credit Lending Operations	3,000	2007
Tempe, AZ	Franchise Lending Operations	3,920	2005
Spokane, WA	Real Estate Lending	1,202	2006

For additional information regarding our premises, see Item 8. Financial Statements and Supplementary Data Notes to Consolidated Financial Statements - Note 7 .

Management believes that ITLA Capital's present facilities are adequate for its current needs, and that alternative or additional space, if necessary, will be available on reasonable terms.

Item 3. Legal Proceedings

We are party to certain legal proceedings incidental to our business. Management believes that the outcome of such proceedings, in the aggregate, will not have a material effect on our business, financial condition or results of operations.

Item 4. Submission of Matters to a Vote of Security Holders

No matter was submitted to a vote of security holders, through the solicitation of proxies or otherwise, during the quarter ended December 31, 2003.

Table of Contents**PART II****Item 5. Market for Registrant's Common Equity and Related Stockholder Matters**

Our common stock is traded on the NASDAQ national market system under the symbol ITLA. As of March 8, 2004, there were nine holders of record of our common stock representing an estimated 1,000 beneficial shareholders with a total of 6,268,673 shares outstanding. We have not paid any cash dividends since our holding company reorganization in 1996. As a bank holding company, our ability to pay dividends may be affected by regulations, including those governing the payment of dividends by the Bank to the Company, which could be a source of funds for any dividends paid by the Company, as well as by the policies of the Federal Reserve Board. See Item 1. Business Regulation and Note 17 to our consolidated financial statements included in Item 8 of this report.

The following table sets forth, for the periods indicated, the range of high and low trade prices for our common stock. Stock price data on NASDAQ reflects inter-dealer prices, without retail mark-up, mark-down or commission.

	Market Price			Average Daily Closing Price
	High	Low	Close	
2003				
4th Quarter	\$51.10	\$44.16	\$50.10	\$48.02
3rd Quarter	45.23	40.20	42.64	42.77
2nd Quarter	40.09	32.98	40.09	37.07
1st Quarter	35.29	31.23	33.04	33.18
2002				
4th Quarter	\$36.25	\$26.37	\$33.23	\$31.36
3rd Quarter	31.25	27.18	30.19	29.66
2nd Quarter	31.15	25.05	29.69	29.25
1st Quarter	24.75	20.25	24.75	22.39

The following table includes supplementary quarterly operating results and per share information for the past two years. The data presented should be read along with Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations and with Item 8. Financial Statements and Supplementary Data included elsewhere in this report.

Quarterly Operations (Unaudited)

	For the Quarter Ended			
	March 31	June 30	September 30	December 31
(in thousands except per share amounts)				
2003				
Interest income	\$33,524	\$27,911	\$27,075	\$27,467
Interest expense	8,433	7,873	7,115	7,446
Net interest income before provision for loan losses	25,091	20,038	19,960	19,878
Provision for loan losses	4,500	1,850	750	660
Non-interest income	12,536	1,241	777	686
General and administrative expense	10,117	8,917	8,958	8,723
Total real estate owned expense, net	143	51	609	409
Provision for income taxes	8,326	3,525	3,473	3,622
Net income	13,022	5,490	5,406	5,716
Basic earnings per share	\$ 2.17	\$ 0.91	\$ 0.90	\$ 0.94
Diluted earnings per share	\$ 2.02	\$ 0.85	\$ 0.83	\$ 0.87
2002				

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Interest income	\$27,035	\$26,570	\$27,380	\$29,623
Interest expense	10,489	9,076	8,800	8,957
Net interest income before provision for loan losses	16,546	17,494	18,580	20,666
Provision for loan losses	1,325	2,100	2,700	2,905
Non-interest income	125	102	(54)	200
General and administrative expense	6,318	6,312	6,459	7,943
Total real estate owned expense, net	467	508	71	277
Provision for income taxes	3,043	3,074	3,326	3,345
Net income	4,719	4,805	5,155	5,326
Basic earnings per share	\$ 0.79	\$ 0.80	\$ 0.86	\$ 0.89
Diluted earnings per share	\$ 0.74	\$ 0.75	\$ 0.80	\$ 0.84

Table of Contents**Item 6. Selected Financial Data**

The following condensed consolidated statements of operations and financial condition and selected performance ratios as of December 31, 2003, 2002, 2001, 2000, and 1999 and for the years then ended have been derived from our audited consolidated financial statements. The information below is qualified in its entirety by the detailed information included elsewhere herein and should be read along with Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations and Item 8. Financial Statement and Supplementary Data.

	As of and for the years ended December 31,				
	2003	2002	2001	2000	1999
(in thousands except per share amount)					
Condensed Consolidated Statements of Operations					
Total interest income	\$ 115,977	\$ 110,608	\$ 123,095	\$ 123,775	\$ 101,213
Total interest expense	30,867	37,322	63,863	68,642	48,460
Net interest income before provisions for loan losses	85,110	73,286	59,232	55,133	52,753
Provision for loan losses	7,760	9,030	4,575	4,775	4,950
Net interest income after provision for loan losses	77,350	64,256	54,657	50,358	47,803
Non-interest income	15,240	373	1,059	2,331	901
Non-interest expense:					
Compensation and benefits	18,870	13,954	11,778	9,958	9,739
Occupancy and equipment	4,839	3,165	2,968	2,567	2,788
Other general and administrative expenses	13,006	9,913	8,072	8,129	8,230
Real estate owned expense, net	1,212	1,323	387	138	472
Total recurring non-interest expense	37,927	28,355	23,205	20,792	21,229
Nonrecurring expense				1,400(1)	
Total non-interest expense	37,927	28,355	23,205	22,192	21,229
Income before provision for income taxes and minority interest in income of subsidiary	54,663	36,274	32,511	30,497	27,475
Minority interest in income of subsidiary(2)(3)	6,083	3,481	2,967	478	
Income before provision for income taxes	48,580	32,793	29,544	30,019	27,475
Provision for income taxes	18,946	12,788	11,393	11,880	11,270
NET INCOME	\$ 29,634	\$ 20,005	\$ 18,151	\$ 18,139	\$ 16,205
BASIC EARNINGS PER SHARE	\$ 4.91	\$ 3.35	\$ 2.82	\$ 2.57	\$ 2.26
DILUTED EARNINGS PER SHARE	\$ 4.55	\$ 3.16	\$ 2.72	\$ 2.51	\$ 2.21
Dividends paid	\$	\$	\$	\$	\$

Condensed Consolidated Statements of Financial Condition

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Cash and cash equivalents	\$ 178,318	\$ 160,848	\$ 134,241	\$ 70,950	\$ 72,242
Investment securities available for sale, at fair value	53,093	54,677	29,411	46,325	59,247
Stock in Federal Home Loan Bank	17,966	16,934	13,464	3,963	8,894
Loans, net	1,436,849	1,316,298	1,122,370	1,045,927	951,480
Real estate loans held in trust, net	68,575	121,936	162,158	211,722	
Interest receivable	8,958	9,158	11,144	11,821	7,383
Other real estate owned, net	7,048	12,593	13,741	2,250	1,041
Premises and equipment, net	5,766	4,197	2,177	2,690	3,253
Deferred income taxes	11,609	13,822	11,869	11,302	9,401
Goodwill	3,118	3,118			
Other assets	26,915	8,384	7,733	8,193	2,882
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total Assets	\$1,818,215	\$1,721,965	\$1,508,308	\$1,415,143	\$1,115,823
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Deposit accounts	\$1,147,017	\$1,065,911	\$ 953,654	\$1,015,699	\$ 913,613
Collateralized mortgage obligations	15,868	69,077	109,648	161,852	
Federal Home Loan Bank advances	362,135	338,685	269,285	79,250	67,250
Account payable and other liabilities	19,696	10,006	9,674	11,269	11,265
Junior subordinated debentures (3)	86,600				
Guaranteed preferred beneficial interests in the Company's junior subordinated deferrable interest debentures (3)		81,595	28,118	13,519	
Shareholders' equity	186,899	156,691	137,929	133,554	123,695
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total Liabilities and Shareholders' Equity	\$1,818,215	\$1,721,965	\$1,508,308	\$1,415,143	\$1,115,823
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Book value per share	\$ 31.30	\$ 27.11	\$ 23.54	\$ 20.05	\$ 17.22
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>

(1) Represents expenses related to the consolidation of the Bank's headquarters with ITLA Capital's headquarters in La Jolla, California.

(2) Represents accrued distributions payable on our trust preferred securities. (3) As a result of our adoption as of December 31, 2003 of revised Interpretation No. 46 issued by the Financial Accounting Standards Board, we de-consolidated our trust subsidiaries which issued our trust preferred securities. The effect of this was to recognize investments in our trust subsidiaries in other assets, to

report the amount of junior subordinated debentures we issued to these trusts as a liability in our consolidated balance sheet and to recognize the interest expense on the junior subordinated debentures in our consolidated statement of income. Prior to the de-consolidation, we reported our trust preferred securities in

Table of Contents

the mezzanine section of our balance sheet as guaranteed preferred beneficial interests in the Company's junior subordinated deferrable interest debentures and recognized distributions paid to the holders of the trust preferred securities as minority interest in income of subsidiary in our consolidated statement of income. See Note 1 to our consolidated financial statements included in Item 8 of this report.

As of and for the years ended December 31,

	2003	2002	2001	2000	1999
Selected Performance Ratios					
Return on average assets	1.71%	1.41%	1.32%	1.47%	1.57%
Return on average shareholders' equity	16.88%	13.56%	13.28%	13.95%	14.23%
Net interest margin (1)	5.03%	5.30%	4.33%	4.47%	5.11%
Average interest-earning assets to average interest bearing liabilities	135.03%	113.94%	113.80%	113.49%	113.74%
Efficiency ratio (2)	37.79%	38.50%	38.49%	38.62%	39.57%
Efficiency ratio excluding real estate operations and nonrecurring expense, net	36.59%	36.70%	37.85%	35.94%	38.69%
Total recurring general and administrative expense to average assets	2.29%	1.90%	1.66%	1.78%	2.01%
Average shareholders' equity to average assets	11.16%	10.36%	9.93%	10.86%	11.01%
Nonperforming assets to total assets	0.86%	1.08%	1.92%	1.44%	0.81%
Allowance for loan losses to loans held for investment, net (3)	2.14%	2.31%	2.16%	2.12%	2.05%
Allowance for loan loss to nonaccrual loans	392.26%	555.61%	174.30%	149.85%	249.40%
Net charge-offs (recoveries) to average loans held for investment, net	0.52%	0.36%	0.39%	0.18%	0.20%

(1) Net interest margin represents net interest income divided by total average interest-earning assets.

(2) Efficiency ratio represents non-interest expense divided by non-interest income and net interest income before provision for loan losses. (3) Loans before allowance for loan losses and net of unearned finance charges and loan fees.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**Application of Critical Accounting Policies and Accounting Estimates**

The accounting and reporting policies followed by the Company conform, in all material respects, to accounting principles generally accepted in the United States and to general practices within the financial services industry. The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. While the Company bases estimates on historical experience, current information

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

and other factors deemed to be relevant, actual results could differ from those estimates.

We consider accounting estimates to be critical to reported financial results if (i) the accounting estimate requires management to make assumptions about matters that are highly uncertain and (ii) different estimates that management reasonably could have used for the accounting estimate in the current period, or changes in the accounting estimate that are reasonably likely to occur from period to period, could have a material impact on the Company's financial statements. Accounting policies related to the allowance for loan losses are considered to be critical, as these policies involve considerable subjective judgment and estimation by management. The Company also considers accounting policies related to stock-based compensation to be critical due to the continuously evolving standards, changes to which could materially impact the way the Company accounts for stock options. We also consider our accounting policies related to our tax refund lending program and other real estate owned to be critical due to the potential significance of these activities and the estimates involved. Critical accounting policies, and the Company's procedures related to these policies, are described in detail below. Also see Note 1 Organization and Summary of Significant Accounting Policies in the accompanying notes to the consolidated financial statements included elsewhere in this report.

Allowance for Loan Losses (ALL). Our management assesses the adequacy of the ALL prior to the end of each calendar quarter. This assessment includes procedures to estimate the allowance and test the adequacy and appropriateness of the resulting balance.

Table of Contents

We establish the ALL amount separately for two different risk groups (1) individual loans (loans with specifically identifiable risks); and (2) homogeneous loans (groups of loan with similar characteristics). We base the allocation for specific loans primarily on risk rating grades assigned to each of these loans as a result of our loan management and review processes. We then assign each risk-rating grade a loss ratio, which is determined based on the experience of management and our independent loan review process. We estimate losses on impaired loans based on estimated cash flows discounted at the loan's original effective interest rate or based on the underlying collateral value. Based on management's experience, we also assign loss ratios to groups of loans. These loss ratios are assigned to the various homogenous categories of the portfolio.

We then test the resulting ALL balance by comparing the balance in the ALL to historical trends and peer information. Our management then evaluates the result of the procedures performed, including the result of our testing, and concludes on the appropriateness of the balance of the ALL in its entirety.

Stock-based Compensation. The Company accounts for stock-based employee compensation plans based on the intrinsic value method provided in Accounting Principles Board Opinion (APB) No. 25, Accounting for Stock Issued to Employees, and related Interpretations. Because the exercise price of the Company's employee and director stock options equals the market price of the underlying stock on the date of grant, no compensation expense is recognized on options granted.

SFAS No. 123, Accounting for Stock-Based Compensation, as amended by SFAS 148, requires pro forma disclosures of net income and earnings per share for companies not adopting its fair value accounting method for stock-based employee compensation. The pro forma disclosures presented in Note 1 - Organization and Summary of Significant Accounting Policies in the accompanying notes to consolidated financial statements included elsewhere in this report use the fair value method of SFAS 123 to measure compensation expense for stock-based employee compensation plans. The fair value of stock options granted was estimated at the date of grant using the Black-Scholes option-pricing model. This model was developed for use in estimating the fair value of publicly traded options that have no vesting restrictions and are fully transferable. Additionally, the model requires the input of highly subjective assumptions. Because the Company's employee and director stock options have characteristics significantly different from those of publicly traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the Black-Scholes option-pricing model does not necessarily provide a reliable single measure of the fair value of the Company's employee stock options.

Tax Refund Lending. In connection with our agreement with Household related to the RAL program, we originate tax refund anticipation loans and sell a non-recourse interest to Household. The non-recourse interest sold represents substantially all of the outstanding loan balance. Premiums earned on the sale of these loans are recorded as income at the time the loans are sold to Household.

Other Real Estate Owned. Properties acquired through foreclosure, or in lieu of foreclosure, are transferred to the other real estate owned portfolio and is initially recorded at estimated fair value less the estimated costs to sell the property. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of cost or estimated fair value less the estimated costs of disposition. The fair value of other real estate owned is generally determined from appraisals obtained from independent appraisers.

Adoption of Recent Accounting Pronouncements

In November 2002, Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 45 (FIN 45), Guarantor's Accounting and Disclosure Requirement for Guarantees, Including Indirect Guarantees of Indebtedness of Others. FIN 45 elaborates on the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. It also clarifies that a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. The initial recognition and measurement provisions for FIN 45 are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. The disclosure requirements of FIN 45 are effective for financial statements of interim or annual periods ending after December 15, 2002, and were included in the Company's financial statements for the years ended December 31, 2003. Implementation of the provisions of FIN 45 did not have a material impact on the Company's financial statements.

Table of Contents

In January 2003, FASB issued FASB Interpretation No. 46 (FIN 46), Consolidation of Variable Interest Entities. FIN 46 establishes the criteria used to identify variable interest entities and to determine whether or not to consolidate a variable interest entity. The Company adopted FIN 46 at December 31, 2003. In accordance therewith, the Company deconsolidated its trusts subsidiaries. The result was to recognize investments in the trusts in other assets, and to report the amount of subordinated debentures issued by the Company to the trusts subsidiaries in the liability section of the Company's consolidated balance sheet. In addition, beginning January 1, 2004, the Company will recognize the interest expense on the subordinated debentures in the consolidated statements of income. Prior to FIN 46, the Company consolidated its trusts subsidiaries and reported trust preferred securities in the mezzanine section of the Company's consolidated balance sheets and recognized the proportionate share of income attributable to the preferred shareholders as minority interest in income of subsidiary in the consolidated statements of income. This interpretation was effective immediately for variable interest entities created after January 31, 2003 and was initially to be effective for variable interest entities acquired prior to February 1, 2003, in the quarter ended September 30, 2003. Effective October 9, 2003, the FASB agreed to defer the effective date of FIN 46 for variable interests held by public companies in all entities that were acquired prior to February 1, 2003. The deferral required public companies to adopt the provisions of FIN 46 for periods ended after December 15, 2003. Adoption of FIN 46, as revised, did not have a material impact on the results of operations or financial position, but will affect net interest income, our efficiency ratios and our net interest spread. As a result of the adoption of FIN 46 at December 31, 2003, financial information prior to the adoption has not been restated.

On May 15, 2003, FASB issued SFAS No. 150, Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity. SFAS 150 modifies the accounting for certain financial instruments that issuers could account for as equity. Under SFAS 150, those instruments with characteristics of both liabilities and equity must be classified as liabilities in the consolidated balance sheets, with the corresponding payments to holders of the instruments recognized as interest expense.

The reporting requirements of SFAS 150 are effective July 1, 2003. On October 29, 2003, the FASB agreed to defer provisions related to mandatory redeemable financial instruments to periods beginning after December 15, 2004. The adoption SFAS 150 did not have a material impact on the results of operations or the financial position of the Company.

General

The following discussion and analysis reviews the financial condition and results of our consolidated operations, including our consolidated subsidiaries: Imperial Capital Bank and Imperial Capital Real Estate Investment Trust.

The following discussion and analysis is intended to identify the major factors that influenced our financial condition as of December 31, 2003 and 2002 and our results of operations for the years ended December 31, 2003, 2002 and 2001. Our primary business involves the origination and purchase of loans secured by income producing real estate, located predominately in California and, to a lesser extent, the origination and purchase of franchise loans and the origination of film finance loans.

Consolidated net income in 2003 was \$29.6 million, or \$4.55 per diluted share, compared to \$20.0 million, or \$3.16 per diluted share in 2002 and \$18.2 million, or \$2.72 per diluted share in 2001. The increase in net income in 2003 was primarily due to an increase in net interest income to \$85.1 million for 2003 as compared to \$73.3 million in 2002, and an increase in non-interest income to \$15.2 million for 2003 as compared to \$373,000 for 2002. These increases were partially offset by a \$9.6 million increase in non-interest expense, a \$2.6 million increase in minority interest in income of subsidiary, and a \$6.2 million increase in provision for income taxes.

The increase in net income in 2002 was primarily due to an increase in net interest income to \$73.3 million for 2002 as compared to \$59.2 million in 2001. This increase was partially offset by a \$4.5 million increase in provision for loan losses and a \$5.2 million increase in non-interest expense.

Total loan production including the unfunded portion of construction loans was \$794.8 million for the year ended December 31, 2003, as compared to \$666.9 million and \$502.1 million for the years ended December 31, 2002 and 2001. Loan production in 2003 consisted of real estate loan originations of \$646.7 million, the origination of \$90.5 million of film finance loans and the origination and purchase of \$57.6 million of franchise loans.

Our average total assets increased approximately 21.5% during 2003 to \$1.7 billion. Average deposit accounts totaled \$1.0 billion in 2003 compared to \$931.4 million in 2002, an increase of \$79.6 million, or 8.6%. FHLB advances averaged \$201.4 million in 2003, compared to \$194.2 million in 2002, an increase of \$7.2 million, or 3.7%. The average balance of the CMOs was \$44.7 million during 2003 compared to \$88.5 million in 2002 reflecting repayments of loans held in trust.

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Table of Contents

As discussed further in the new accounting pronouncement section above, we deconsolidated our trusts subsidiaries as of December 31, 2003. As a result, we recorded the \$86.6 million of underlying debentures issued by us to the trusts subsidiaries as Junior subordinated debentures and \$2.6 million of our investment in the trusts and \$2.1 million of deferred debt issuance costs as Other assets in the consolidated balance sheet at December 31, 2003. Further discussion of the trust subsidiaries and related junior subordinated debentures is included in Notes 1 and 10 to the consolidated financial statements included in Item 8 of this report.

Results of Operations

Net Interest Income

The following table presents, for the periods indicated, our condensed average balance sheet information, together with interest income and yields earned on average interest-earning assets and interest expense and rates paid on average interest-bearing liabilities. Average balances are computed using daily average balances. Nonaccrual loans are included in loans receivable.

	Years Ended December 31,								
	2003			2002			2001		
	Average Balance	Income/ Expense	Yield/ Rate	Average Balance	Income/ Expense	Yield/ Rate	Average Balance	Income/ Expense	Yield/ Rate
(dollars in thousands)									
Assets									
Cash and investment securities	\$ 277,832	\$ 5,399	1.94%	\$ 77,384	\$ 3,475	4.49%	\$ 73,823	\$ 3,192	4.32%
Real estate loans (I)	1,145,177	89,327	7.80%	1,083,645	91,066	8.40%	1,072,792	102,233	9.53%
Real estate loans held in trust (I)	97,698	5,980	6.12%	143,705	10,239	7.13%	189,349	14,954	7.90%
Franchise loans (I)	66,101	4,772	7.22%	60,492	4,479	7.40%	32,956	2,716	8.24%
Motion picture financing (I)	99,104	7,433	7.50%	18,060	1,349	7.47%			
Commercial and other loans (I)	7,732	3,066	39.65%						
Total loans receivable	1,415,812	110,578	7.81%	1,305,902	107,133	8.20%	1,295,097	119,903	9.26%
Total interest earning assets	1,693,644	\$ 115,977	6.85%	1,383,286	\$ 110,608	8.00%	1,368,920	\$ 123,095	8.99%
Non-interest-earning assets	70,226			70,468			34,218		
Allowance for loan losses	(33,508)			(30,071)			(26,835)		
Total assets	\$ 1,730,362			\$ 1,423,683			\$ 1,376,303		
Liabilities and Shareholders Equity									
Interest bearing deposit accounts:									
Interest demand accounts	\$ 12,571	\$ 136	1.08%	\$	\$		\$	\$	
Money market and passbook accounts	162,638	2,551	1.57%	151,258	2,873	1.90%	119,022	4,767	4.01%
Time certificates	832,873	21,929	2.63%	780,168	26,476	3.39%	841,002	48,097	5.72%
Total interest bearing deposit accounts	1,008,082	24,616	2.44%	931,426	29,349	3.15%	960,024	52,864	5.51%
Collateralize mortgage obligations	44,767	1,076	2.40%	88,485	2,301	2.60%	139,267	6,209	4.46%
FHLB Advances	201,419	5,175	2.57%	194,160	5,672	2.92%	103,675	4,790	4.62%
Total interest bearing liabilities	1,254,268	\$ 30,867	2.46%	1,214,071	\$ 37,322	3.07%	1,202,966	\$ 63,863	5.31%

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Non-interest bearing demand accounts	2,973			
Other non-interest bearing liabilities	297,549	62,080	36,644	
Shareholders equity	175,572	147,532	136,693	
Total liabilities and shareholders equity	\$ 1,730,362	\$ 1,423,683	\$ 1,376,303	
Net interest spread (2)		4.39%	4.93%	3.68%
Net interest income before provisions for loan losses	\$ 85,110	\$ 73,286	\$ 59,232	
Net interest margin (3)		5.03%	5.30%	4.33%

(1) Before allowance for loan losses and net of deferred loan fees and costs. Net loan fee amortization of \$2.4 million, \$1.7 million and \$1.3 million was included in net interest income for 2003, 2002 and 2001, respectively.

(2) Average yield on interest-earning assets minus average rate paid on interest-bearing liabilities.(3) Net interest income divided by total average interest-earning assets.

Our primary source of revenue is net interest income. Our net interest income is affected by (a) the difference between the yields recognized on interest-earning assets, including loans and investments, and the interest rates paid on interest-bearing liabilities, which is referred to as net interest spread, and (b) the relative amounts of interest-earning assets and interest-bearing liabilities. As of December 31, 2003, 2002 and 2001, our ratio of average interest-earning assets to average interest-bearing liabilities was 135.03%, 113.93% and 113.80%, respectively.

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Table of Contents

The following table sets forth a summary of the changes in interest income and interest expense resulting from changes in average interest-earning asset and interest-bearing liability balances and changes in average interest rates. The change in interest due to both volume and rate has been allocated to change due to volume and rate in proportion to the relationship of the absolute dollar amounts of each.

	2003 vs. 2002			2002 vs. 2001		
	Increase (Decrease) Due to:			Increase (Decrease) Due to:		
	Volume	Rate	Total	Volume	Rate	Total
(in thousands)						
Interest and fees earned on:						
Loans, net	\$ 12,373	\$ (4,669)	\$ 7,704	\$ 4,695	\$ (12,750)	\$ (8,055)
Cash and investment securities	3,894	(1,970)	1,924	159	124	283
Real estate loans held in trust	(2,810)	(1,449)	(4,259)	(3,256)	(1,459)	(4,715)
Total increase (decrease) in interest income	13,457	(8,088)	5,369	1,598	(14,085)	(12,487)
Interest paid on:						
Deposit accounts	1,944	(6,677)	(4,733)	(899)	(22,616)	(23,515)
Collateralized mortgage obligations	(1,048)	(177)	(1,225)	(1,319)	(2,589)	(3,908)
FHLB advances	186	(683)	(497)	2,644	(1,762)	882
Total increase (decrease) in interest expense	1,082	(7,537)	(6,455)	426	(26,967)	(26,541)
Increase (decrease) net interest income	\$ 12,375	\$ (551)	\$ 11,824	\$ 1,172	\$ 12,882	\$ 14,054

2003 Compared to 2002

Net interest income before provision for loan losses increased to \$85.1 million for the year ended December 31, 2003, compared to \$73.3 million for the prior year, an increase of 16.1%. This increase was due primarily to increased net interest income of the Bank offset by the decline in the net interest income of the REIT. The Bank's net interest income improved from the prior year primarily as a result of the increase in the average balance of loans outstanding and a decline in the average cost of funds due to its interest bearing liabilities repricing to lower current market interest rates. The increase in the Bank's net interest income was partially offset by a decline in the yield of its loan portfolio as higher yielding loans were repaid and replaced by new loan production at lower current market interest rates.

The average yield on our total loan portfolio was 7.81% in 2003 compared to 8.20% in 2002. Our commercial real estate loan portfolio is primarily composed of adjustable rate mortgages indexed to six month LIBOR with interest rate floors, below which the loan's contractual interest rate may not adjust. Approximately 95.4% of our real estate loan portfolio (including real estate loans held in trust) was comprised of adjustable rate mortgages at December 31, 2003. These adjustable rate mortgages generally re-price on a quarterly basis and, as of December 31, 2003, approximately \$1.3 billion or 96.5% of our real estate loan portfolio contained interest rate floors, below which the loan's contractual interest rate may not adjust. At December 31, 2003, the weighted average floor interest rate of these loans was 6.83%. At that date, approximately \$1.2 billion or 93.6% of those loans were at the floor interest rate.

Net interest income was also positively impacted by an increased interest income from cash and investment securities as a result of increased liquidity in connection with the Bank's RAL program with Household.

The net interest income of the REIT declined from the prior year as a result of the reduction in the average balance of its loan portfolio, caused by a significant increase in loan prepayments, and a decline in its net interest spread due to its assets repricing to lower current market interest rates slightly faster than its liabilities.

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Interest expense on interest-bearing liabilities decreased \$6.5 million or 17.3% to \$30.9 million in 2003 compared to \$37.3 million in 2002 primarily due to a decrease in interest expense on deposits and CMOs. Interest expense from deposit accounts decreased \$4.7 million or 16.1% to \$24.6 million in 2003 compared to \$29.3 million in 2002 due to decreases in the average rate paid on deposits as a result of lower market interest rates and the growth in retail non-interest bearing demand deposits in 2003. The average rate paid on deposits was 2.44% in 2003 compared to 3.15% in 2002.

Interest expense from the CMOs decreased \$1.2 million or 53.2% to \$1.1 million in 2003 as compared to \$2.3 million in 2002. The decrease was primarily due to a decrease in rates paid on CMOs, as well as a decline in average balance of CMOs. The average balance and average yield on the CMOs was \$44.8 million and 2.40%, respectively, in 2003 as compared to \$88.5 million and 2.60% in 2002, respectively.

Table of Contents

Interest expense from FHLB advances decreased \$497,000 to \$5.2 million in 2003 compared to \$5.7 million in 2002, due to a decrease in the average rate paid on FHLB advances. The average balance of FHLB advances increased \$7.3 million or 3.7% to \$201.4 million in 2003 compared to \$194.2 million in 2002. The average rate paid on FHLB advances was 2.57% in 2003 compared to 2.92% in 2002. We have used our borrowing capacity under our FHLB credit line to take advantage of the current favorable short-term rate environment through effective liability management, which has lowered our cost of funds and enhanced our net interest income.

Provision for Loan losses

Provision for loan losses decreased to \$7.8 million in 2003 compared to \$9.0 million in 2002. The current period provision for loan losses was recorded to provide reserves adequate to support the known and inherent risk of loss in the loan portfolio, and reflects the overall decline in total non-performing loans and other loans of concern from \$41.4 million at December 31, 2002 to \$39.8 million at December 31, 2003. See also Credit Risk Elements Allowance for Loan Losses and Nonperforming Assets .

Non-interest Income

Non-interest income increased \$14.9 million to \$15.2 million in 2003 compared to \$0.4 million in 2002. The increase in non-interest income was due primarily to fee income earned in connection with the RAL program, consisting of approximately \$9.0 million of net premiums on the sale of RAL loans and \$4.6 million of processing and administrative fees. Because the RAL program relates to the filing of income tax returns, transaction activity is concentrated during the tax season. This resulted in the Company earning substantially all of its RAL program income in the first quarter of the year.

Non-interest Expense

General and Administrative Expense

General and administrative expenses increased to \$36.7 million for the current year, compared to \$27.0 million for the previous year. The increase was attributable to the acquisition of the LHO, the development of Imperial Capital Express (the Bank's small balance commercial real estate lending platform), additions to the Bank's franchise loan origination staff, and certain infrastructure and personnel costs relating to the Bank's charter conversion. The Company's efficiency ratio (defined as recurring general and administrative expenses as a percentage of net revenue) was 36.6 percent for the year ended December 31, 2003, compared to 36.7 percent for the prior year. Full time equivalent associates averaged 209 in 2003 compared to 154 in 2002.

Real Estate Owned Expense

Real estate owned expense, decreased to \$1.2 million in 2003 compared to \$1.3 million in 2002. The decrease was primarily attributable to a \$250,000 decrease in real estate owned expenses, partially offset by an increase of \$74,000 in the provision for losses on other real estate owned (OREO) and a decrease of \$65,000 in gain on sale of OREO, net. See also Credit Risk Elements Allowance for Loan Losses and Nonperforming Assets .

Income Taxes

Provision for income taxes increased to \$18.9 million in 2003 compared to \$12.8 million in 2002. The increase in provision for income taxes was due to the increase in taxable income earned in 2003. The effective tax rate was 39.0% for 2003 and 2002. The effective tax rate differed from the applicable statutory federal tax rate due to state income taxes and the state income tax deduction for tax exempt income on loans located in designated redevelopment and enterprise zones and due to federal income tax credits received from a low income housing tax credit investment.

At December 31, 2003, we had a net deferred tax asset of \$11.6 million. The deferred tax asset related primarily to loan loss provisions recognized on our financial statements that have not yet been recognized on our income tax returns. During 2003, we had no deferred tax assets relating to net operating loss carry forward deductions. The deferred tax asset is considered fully realizable. Accordingly, no valuation allowance on the deferred tax asset was established in 2003.

Minority Interest in Income of Subsidiary

Minority interest in income of subsidiary, consisting of accrued distributions payable on our Trust Preferred securities, was \$6.1 million in 2003 as compared to \$3.5 million in 2002. The increase was due to the issuance of \$55.0 million of variable rate cumulative

Table of Contents

Trust Preferred securities during the fourth quarter of 2002, which were outstanding for the entire year in 2003. See Item 8. Financial Statements and Supplementary Data Notes to Consolidated Financial Statements Note 10 .

2002 Compared to 2001

Net interest income before provision for loan losses increased \$14.1 million or 23.8% to \$73.3 million in 2002 compared to \$59.2 million in 2001. The increase in net interest income was primarily attributable to the improvement in net interest spread caused by the declining rate environment, which lowered our average cost of funds and resulted in most of our loans reaching their interest rate floors.

Interest income decreased \$12.5 million or 10.1% to \$110.6 million in 2002 compared to \$123.1 million in 2001. The decrease in interest income was due primarily to our loans being originated or repricing at lower rates due to the general decline in market interest rates. The average yield on our loans was 8.40% in 2002 compared to 9.53% in 2001. Our commercial real estate loan portfolio is primarily comprised of adjustable rate mortgages indexed to the six month LIBOR. Approximately 91.6% of our real estate loan portfolio (including real estate loans held in trust) was adjustable rate mortgages at December 31, 2002. These adjustable rate mortgages generally re-price on a quarterly basis and, as of December 31, 2002, approximately \$1.1 billion or 87.1% of our real estate loan portfolio contained interest rate floors, below which the loans contractual interest rate may not adjust. At December 31, 2002, the weighted average floor interest rate of these loans was 7.45%. At that date, approximately \$1.1 billion or 97.9% of those loans were at the floor interest rate.

Interest expense on interest-bearing liabilities decreased \$26.5 million or 41.6% to \$37.3 million in 2002 compared to \$63.9 million in 2001 primarily due to a decrease in interest expense on deposits and CMOs. Interest expense from deposit accounts decreased \$23.5 million or 44.5% to \$29.3 million in 2002 compared to \$52.9 million in 2001 due to decreases in the average rate paid on deposits as a result of lower market interest rates. The average rate paid on deposits was 3.15% in 2002 compared to 5.51% in 2001.

Interest expense from the CMOs decreased \$3.9 million or 62.9% to \$2.3 million in 2002 as compared to \$6.2 million in 2001. The decrease was primarily due to a decrease in rates paid on CMOs, as well as a decline in average balance of CMOs. The average balance and average yield on the CMOs was \$88.5 million and 2.60% in 2002 as compared to \$139.3 million and 4.46% in 2001, respectively.

Interest expense from FHLB advances increased \$0.9 million to \$5.7 million in 2002 compared to \$4.8 million in 2001, due to an increase in the average outstanding balance, which was partially offset by a decrease in the average rate paid on FHLB advances. The average balance of FHLB advances increased \$90.5 million or 87.3% to \$194.2 million in 2002 compared to \$103.7 million in 2001. The average rate paid on FHLB advances was 2.92% in 2002 compared to 4.62% in 2001.

Provision for Loan losses

Provision for loan losses increased to \$9.0 million in 2002 compared to \$4.6 million in 2001. The current period provision for loan losses was recorded to provide the reserves adequate to support the known and inherent risk of loss resulting from the current growth in the loan portfolio and due to the increase in other loans of concern to \$35.5 million from \$21.5 million at December 31, 2001. See also Credit Risk Elements Allowance for Loan Losses and Nonperforming Assets .

Non-interest Income

Non-interest income decreased \$0.7 million to \$0.4 million in 2002 compared to \$1.1 million in 2001. The decrease in non-interest income was due primarily to a \$0.5 million net valuation provision recorded in 2002 for the Company s residual interest relating to the securitization of our residential loan portfolio.

Table of Contents

Non-interest Expense

General and Administrative Expense

General and administrative expense totaled \$27.0 million and \$22.8 million in 2002 and 2001, respectively. In 2002, our ratio of recurring general and administrative expenses to average assets was 1.90%, compared to 1.66% in 2001. This increase was primarily attributable to the additions made to the retail and wholesale loan originations sales and support staff, and certain infrastructure costs relating to the charter conversion activities, including core processing system conversion costs, and additions to the information technology and savings and operation staff. Full time equivalent associates averaged 154 in 2002 compared to 133 in 2001.

Real Estate Owned Expense

Real estate owned expense, net, increased to \$1.3 million in 2002 compared to \$0.4 million in 2001. The increase was primarily attributable to a \$0.5 million increase in real estate owned expense and to the \$0.5 million increase in the provision for losses on OREO. These increases were offset by a \$0.1 million increase in gain on sale of OREO, net. See also *Credit Risk Elements* Allowance for Loan Losses and Nonperforming Assets .

Income Taxes

Provision for income taxes increased to \$12.8 million in 2002 compared to \$11.4 million in 2001. The increase in provision for income taxes was primarily due to an increase in taxable income. The effective tax rate was 39.0% and 38.6% for 2002 and 2001, respectively. The effective tax rate differed from the applicable statutory federal tax rate due to state income taxes and the state income tax deduction for tax exempt income on loans located in designated redevelopment and enterprise zones and due to federal income tax credits received from a low income housing tax credit investment.

At December 31, 2002, we had a net deferred tax asset of \$13.8 million. The deferred tax asset related primarily to loss provisions recognized on our financial statements that have not yet been recognized on our income tax returns. During 2002, we had no deferred tax assets relating to net operating loss carry forward deductions. The deferred tax asset is considered fully realizable, as when the temporary differences associated with the deferred tax assets are recognized for income tax purposes, those deductions are expected to be fully offset, either by carryback against previously taxed income or by a reduction of future taxable income. Accordingly, no valuation allowance on the deferred tax asset was established in 2002.

Minority Interest in Income of Subsidiary

Minority interest in income of subsidiary, consisting of accrued distributions payable on our Trust Preferred securities, was \$3.5 million in 2002 as compared to \$3.0 million in 2001. The increase was due to the additional issuance of \$55.0 million of variable rate cumulative Trust Preferred securities in 2002, as well as the Trust Preferred securities issued in 2001 being outstanding for the entire fiscal year in 2002. See *Item 8. Financial Statements and Supplementary Data* Notes to Consolidated Financial Statements Note 10 .

Financial Condition

At December 31, 2003 Compared with December 31, 2002

Total assets increased by \$96.3 million, or 5.6%, to \$1.8 billion at December 31, 2003 compared to \$1.7 billion at December 31, 2002. This increase was primarily due to a \$17.5 million, or 10.9%, increase in cash and cash equivalents to \$178.3 million at December 31, 2003 from \$160.8 million at December 31, 2002, and a \$120.6 million, or 9.2%, increase in loans receivable, net to \$1.4 billion at December 31, 2003 from \$1.3 billion at December 31, 2002. These increases were partially offset by the reductions in net real estate loans held in trust of \$53.4 million. The growth in assets was funded primarily by an increase in deposits of \$81.1 million and in FHLB advances of \$23.5 million. The increase in deposits was primarily related to an increase in interest bearing demand accounts of \$38.5 million and an increase in time certificates of deposit of \$45.5 million. CMOs decreased from \$69.1 million at December 31, 2002 to \$15.9 million at December 31, 2003, reflecting repayments on loans held in trust. Shareholders' equity increased primarily due to the retention of \$29.6 million of net income.

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Table of Contents

At December 31, 2002 Compared with December 31, 2001

Total assets increased by \$213.7 million, or 14.2%, to \$1.7 billion at December 31, 2002 compared to \$1.5 billion at December 31, 2001. This increase was primarily due to a \$26.6 million, or 19.8%, increase in cash and cash equivalents to \$160.8 million at December 31, 2002 from \$134.2 million at December 31, 2001, and a \$193.9 million, or 17.3%, increase in loans receivable, net to \$1.3 billion at December 31, 2002 from \$1.1 billion at December 31, 2001. These increases were partially offset by the reductions in net real estate loans held in trust of \$40.2 million. The growth in assets was funded primarily by an increase in FHLB advances of \$69.4 million and deposits of \$112.3 million. The increase in deposits was primarily concentrated in brokered deposits with a lower cost of funds than the current market rates offered through the Bank's retail branch network. CMOs decreased from \$109.6 million at December 31, 2001 to \$69.1 million at December 31, 2002, reflecting the repayments on loans held in trust. Shareholders' equity increased primarily due to the retention of \$20.0 million of net income as retained earnings for the year, partially offset by the purchase of \$2.3 million of ITLA Capital's common stock currently held as treasury stock.

Loans Receivable, Net

The following table shows the comparison of our loan portfolio by major categories as of the dates indicated.

	December 31,				
	2003	2002	2001	2000	1999
	(in thousands)				
Real estate loans	\$ 1,196,729	\$ 1,189,258	\$ 1,191,688	\$ 1,176,988	\$ 864,048
Construction loans	129,540	101,422	54,129	95,206	107,833
Total real estate loans	1,326,269	1,290,680	1,245,817	1,272,194	971,881
Film finance	98,630	119,283			
Franchise loans	102,128	54,672	57,617	3,912	
Commercial and other loans	6,869	4,314			
	1,533,896	1,468,949	1,303,434	1,276,106	971,881
Unamortized premium	5,429	7,898	9,773	11,300	2,590
Deferred loan origination fees and costs	(500)	(5,604)	(2,029)	(2,571)	(3,096)
	1,538,825	1,471,243	1,311,178	1,284,835	971,375
Allowance for loan losses	(33,401)	(33,009)	(26,650)	(27,186)	(19,895)
	\$ 1,505,424	\$ 1,438,234	\$ 1,284,528	\$ 1,257,649	\$ 951,480

The contractual maturities of our loan portfolio at December 31, 2003 are as follows:

	Loans Maturing in			Total
	Less Than One Year	Between One and Five Years	Greater Than Five Years	
	(dollars in thousands)			
Real estate loans	\$ 50,788	\$ 131,966	\$ 1,013,975	\$ 1,196,729
Construction loans	55,538	48,035	25,967	129,540
Film finance	83,062	15,568		98,630
Franchise loans		12,482	89,646	102,128
Commercial and other loans	6,083	786		6,869

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

	\$ 195,471	\$ 208,837	\$ 1,129,588	\$ 1,533,896
Loans with fixed interest rates	\$ 12,279	\$ 37,900	\$ 16,558	\$ 66,737
Loans with variable interest rates	183,192	170,937	1,113,030	1,467,159
	\$ 195,471	\$ 208,837	\$ 1,129,588	\$ 1,533,896
Percentage with variable interest rates	93.7%	81.9%	98.5%	95.6%

The table above should not be regarded as a forecast of future cash collections because a substantial portion of real estate loans may be renewed or repaid prior to contractual maturity and have adjustable interest rates.

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Table of Contents

The following table sets forth certain information regarding the real property collateral securing our real estate loan portfolio as of December 31, 2003.

	Number of Loans	Gross Amount	Percent of Total	Range of Principal Balance			Non- Accrual Loans
				Min	Max	Average	
(dollars in thousands)							
Income Producing Property Loans:							
Multi-family (5 or more units)	1,209	\$ 675,584	50.94%	\$ 3	\$ 8,178	\$ 578	\$2,557
Retail	121	138,710	10.46%	4	10,456	1,146	
Office	71	106,044	8.00%	18	10,426	1,178	77
Hotel	28	76,619	5.78%	106	11,679	2,736	1,359
Industrial/warehouse	38	31,353	2.36%	9	4,091	825	
Mixed-use	89	79,145	5.97%	27	6,620	889	
Mobile home parks	42	29,500	2.22%	82	1,693	702	
Other	63	55,548	4.19%	23	5,891	882	289
Total income producing	1,661	1,192,503	89.92%				4,282
Construction and Land:							
Construction	43	129,540	9.76%	30	15,149	3,013	
Land	1	1,579	0.12%	1,579	1,579	1,579	
Total construction and land	44	131,119	9.88%				
Single-family mortgages:							
Single-family (1-4 units)	19	2,647	0.20%	11	468	139	404
	1,724	\$ 1,326,269	100.0%				\$4,686

The following table sets forth the location of the collateral for our real estate loan portfolios as of December 31, 2003.

	Number of Loans	Gross Amount	Percent of Total
(dollars in thousands)			
Southern California:			
Los Angeles County	789	\$ 464,223	35.02%
San Diego County	64	92,998	7.01%
Riverside County	48	50,102	3.78%
San Bernardino County	58	48,079	3.62%
Orange County	48	37,443	2.82%
All Other Southern California Counties	22	38,929	2.93%
Total Southern California	1,029	731,774	55.19%
Northern California:			
San Francisco County	21	11,745	0.89%
Sacramento County	3	1,631	0.12%
Santa Clara County	3	7,839	0.59%
Alameda County	41	31,162	2.35%
Fresno County	42	20,946	1.58%
San Mateo	12	8,545	0.64%

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

All Other Northern California Counties	163	149,785	11.29%
	<u> </u>	<u> </u>	<u> </u>
Total Northern California	285	231,653	17.46%
	<u> </u>	<u> </u>	<u> </u>
Outside California:			
Arizona	127	105,440	7.95%
Texas	42	21,757	1.64%
Washington	26	33,015	2.49%
Nevada	62	69,602	5.25%
Colorado	55	50,185	3.78%
Oregon	42	33,326	2.51%
Montana	2	11,863	0.89%
Utah	10	5,952	0.45%
Idaho	5	9,432	0.71%
Other U.S. States	39	22,270	1.68%
	<u> </u>	<u> </u>	<u> </u>
Total Outside California	410	362,842	27.35%
	<u> </u>	<u> </u>	<u> </u>
	1,724	\$ 1,326,269	100.0%
	<u> </u>	<u> </u>	<u> </u>

Table of Contents

Although we generally seek to limit risks associated with our portfolio of real estate and construction loans by limiting the geographic concentration and by varying the types of underlying collateral, significant concentration risks still remain. Concentrations of loans in certain geographic regions, for example, cause our risk associated with these loans to be closely associated with the general economic and social environment of the region. Localized economic and competitive conditions, natural disasters, possible terrorist activities or social conditions all may affect the values of collateral located within a particular geographic area. In addition, certain types of properties may be more or less subject to changes in prevailing economic, competitive or social conditions.

The following table sets forth certain information with respect to our loan originations and purchases. Premiums paid and discounts taken on loans purchased in the secondary market are not included below.

	As of and for the Years Ended December 31,		
	2003	2002	2001
	(dollars in thousands)		
Gross real estate loans originated and retained in the portfolio	\$ 599,885	\$ 412,332	\$ 285,650
Gross real estate loans originated on behalf of third-party investors			9,018
Gross commercial revolving credit loans	41,054	4,195	
Gross film financing originated	90,528	34,340	
Gross franchise loans originated	50,333		
Gross film financing purchased		92,584(1)	
Gross franchise loans purchased	7,244	7,335	53,319
Gross real estate loans purchased	46,809	120,363(1)	154,081
Total loan production	\$ 835,853	\$ 671,149	\$ 502,068
Gross loans at end of period	\$ 1,533,896	\$ 1,468,949	\$ 1,303,434
Gross loans weighted-average portfolio yield	7.64%	8.20%	9.26%
Average size of loans originated and retained in the Company's portfolio	\$ 943	\$ 1,062	\$ 1,120

(1) Includes \$36.8 million of gross real estate loans acquired in 2002 in connection with the acquisition of Asahi Bank of California and \$92.6 million of film finance loans acquired in 2002 in connection with the acquisition of LHO.

Investment Securities

The following table shows the amortized cost and approximate fair value of investment securities available for sale at the dates indicated.

	December 31,					
	2003		2002		2001	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(in thousands)					
U.S. Government Agency	\$47,749	\$47,621	\$48,698	\$48,986	\$29,409	\$29,404
Residual interest in securitized loans	5,055	5,368	5,305	5,619		
Equity securities	25	104	25	72	14	7
Total investment securities available for sale	\$52,829	\$53,093	\$54,028	\$54,677	\$29,423	\$29,411

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

During the first quarter of 2002, the Company formed a limited liability company to issue \$86.3 million of asset-backed notes in a securitization of substantially all of its residential loan portfolio. The Company recognized a gain of \$3.7 million on the securitization of these loans which is included in other non-interest income within the consolidated statements of income for 2002. Concurrent with recognizing such gain on sale, the Company recorded a residual interest of \$5.6 million, which represents the present value of future cash flows (spread and fees) that are anticipated to be received over the life of the loans. The residual interest is recorded on the consolidated balance sheets in the Investment securities available for sale, at fair value. The value of the residual interest is subject to substantial credit, prepayment, and interest rate risk on the sold residential loans. In accordance with the provisions of SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities, the residual interest is classified as available-for-sale and, as such, recorded at fair value with the resultant changes in fair value recorded as unrealized gain or loss in a separate component of shareholders' equity in accumulated other comprehensive income or loss, until realized. Fair value is determined on a monthly

Table of Contents

basis based on a discounted cash flow analysis. These cash flows are projected over the lives of the receivables using prepayment, default, and interest rate assumptions that we believe market participants would use for similar financial instruments.

During 2003, the Company recognized an other than temporary impairment of \$1.0 million in connection with its residual interest. Impairments that are deemed to be other than temporary are charged to non-interest income. In evaluating impairments as other than temporary the Company considers credit risk, as well as the magnitude and trend of default rates and prepayment speeds of the underlying residential loans.

At December 31, 2003 and 2002, key assumptions used to estimate the fair value of the residual interest based on projected cash flows, and the sensitivity of the value to immediate adverse changes in those assumptions is as follows:

	December 31, 2003	December 31, 2002
Dollars in thousands		
Fair value of retained interest	\$ 5,368	\$ 5,619
Weighted average life (in years) securities	0.90	1.49
Weighted average life (in years) residual interest	4.47	4.70
Weighted average annual prepayment speed	35.0%	35.0%
Impact of 10% adverse change	\$ (67)	\$ (23)
Impact of 25% adverse change	\$ (120)	\$ (59)
Weighted average annual discount rate	15.0%	15.0%
Impact of 10% adverse change	\$ (147)	\$ (167)
Impact of 25% adverse change	\$ (367)	\$ (404)
Weighted average lifetime credit losses	3.3%	3.3%
Impact of 10% adverse change	\$ (313)	\$ (285)
Impact of 25% adverse change	\$ (753)	\$ (678)

These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in the fair value of the residual are based on a variation in assumptions and generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, in the above table, the effect of a variation in a particular assumption on the fair value of the residual interest is calculated without changing any other assumption; in reality, changes in one factor may result in changes in another (for example, increases in market interest rates may result in lower prepayments but increased credit losses), which might magnify or counteract the sensitivities, and depending on the severity of such changes, the results of operations may be materially affected.

The following table indicates the composition of the investment security portfolio assuming these securities are held to maturity based on the final maturity of each investment.

	Due in One Year or Less		Due after One Year through Five Years		Due after Five Years through Ten Years		Due after Ten Years	
	Balance	Weighted Average Yield	Balance	Weighted Average Yield	Balance	Weighted Average Yield	Balance	Weighted Average Yield
December 31, 2003								
Investment securities available for sale								
U.S. Government Agency	\$		\$46,791	2.82%	\$		\$830	8.33%
Equity securities	104							
Residual interest in securitized loans			5,368					
	—		—		—		—	
Total investment securities available for sale	\$ 104		\$52,159		\$		\$830	

Liquidity and Deposit Accounts

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Liquidity refers to our ability to maintain cash flow adequate to fund operations and meet obligations and other commitments on a timely basis, including the payment of maturing deposits and the origination or purchase of new loans. We maintain a cash and investment securities portfolio designed to satisfy operating and regulatory liquidity requirements while preserving capital and maximizing yield. As of December 31, 2003 and 2002, the Bank's liquidity ratios were 17.5% and 19.0%, respectively, exceeding the DFI regulatory requirement of 1.5%. In addition, our liquidity position is supported by a credit facility with the FHLB of San Francisco. As of December 31, 2003, we had remaining available borrowing capacity under this credit facility of \$161.0 million, net of the \$8.5 million of additional FHLB Stock that we would be required to purchase to support those additional borrowings, and \$30.0 million of unused federal funds credit facilities under established lines of credit with two banks. In addition, ITLA Capital established two \$25.0 million revolving credit facilities with an unaffiliated bank. Both credit facilities were entered into on January 1, 2004. These facilities mature on March 31, 2004 and January 1, 2005, respectively.

Table of Contents

Total deposit accounts increased approximately \$81.1 million to \$1.147 billion at December 31, 2003 from \$1.066 billion at December 31, 2002. The increase in deposits in 2003 was primarily related to an increase in interest bearing demand deposit accounts of \$38.5 million and an increase in time certificate of deposits of \$45.5 million. Brokered deposits totaled \$126.8 million and \$103.6 million at December 31, 2003 and 2002, respectively. Total deposit accounts increased approximately \$112.3 million to \$1.1 billion at December 31, 2002 from \$953.7 million at December 31, 2001. In both 2003 and 2002, the funds provided from deposits were used to fund the growth in our loan portfolio. Although we compete for deposits primarily on the basis of rates, based on our historical experience regarding retention of deposits, management believes that a significant portion of deposits will remain with us upon maturity on an ongoing basis.

The following table sets forth information regarding deposits outstanding at the dates indicated.

	December 31,		
	2003	2002	2001
	(in thousands)		
Non-interest demand accounts	\$ 9,074	\$	\$
Interest demand accounts	38,518		
Money market and passbook accounts	156,505	168,525	158,188
Time certificates under \$100,000	564,207	521,404	526,911
Time certificates \$100,000 and over	378,713	375,982	268,555
	<u>\$ 1,147,017</u>	<u>\$ 1,065,911</u>	<u>\$ 953,654</u>

The following table sets forth the maturities of certificates of deposit \$100,000 and over at December 31, 2003 (in thousands):

Certificates of deposit \$100,000 and over:	
Maturing within three months	\$ 72,425
After three but within six months	96,517
After six but within twelve months	121,928
After twelve months	87,843
	<u>\$ 378,713</u>

Off-Balance Sheet Arrangements

In the normal course of operations, the Company engages in a variety of financial transactions that, in accordance with generally accepted accounting principles are not recorded in the financial statements. These transactions involve, to varying degrees, elements of credit, interest rate, and liquidity risk. Such transactions are used by the Company to meet the financing needs of our customers.

The Company's off-balance sheet arrangements, which principally include lending commitments, are described below. At December 31, 2003, the Company also had a residual interest of \$5.4 million in a qualified special purpose entity formed in 2002 to issue \$86.3 million of asset-backed notes in a securitization of substantially all of the Company's residential loan portfolio, and a \$2.6 million equity interest in our deconsolidated trusts through which we have issued trust preferred securities. See Notes 10 and 12 of our consolidated financial statements included in Item 8 of this report.

Lending Commitments. Lending commitments include loan commitments, unused lines of credit and standby letters of credit. The instruments are not recorded in the consolidated balance sheet until funds are advanced under the commitments. The Company provides these lending commitments to customers in the normal course of business.

At December 31, 2003, the Company's approved loan origination commitments outstanding totaled \$153.5 million. Unfunded commercial letters of credit and revolving credit lines totaled \$66.1 million. These letters of credit are commitments for possible future extension of credit to existing customers. These lines of credit are typically uncollateralized and usually do not contain a specified maturity date.

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

The Company applies essentially the same credit policies and standards as it does in the lending process when making these commitments. See Note 15 to the consolidated financial statements included in Item 8 of this report for additional information regarding lending commitments.

Table of Contents**Contractual Obligations**

The following table shows the contractual obligations of the Company by expected payment period, as of December 31, 2003. Further discussion of these commitments is included in Notes 8, 10, 11, and 16 to the consolidated financial statements included in Item 8 of this report.

Contractual Obligations	Total	One Year or Less	After One Through Three Years	After Three Through Five Years	More Than Five Years
(in thousands)					
Long-term FHLB advances	\$ 111,135	\$ 56,600	\$ 34,005	\$ 11,000	\$ 9,530
Junior subordinated debentures	86,600				86,600
Operating lease obligations	11,382	2,632	5,281	3,288	181
Deposits with stated maturity dates	942,920	726,191	190,128	26,601	
Purchase obligations	2,470	687	1,783		

FHLB advances and junior subordinated debentures have defined terms and under certain circumstances are callable at the option of the lender.

Operating leases represent obligations entered into by the Company for its use of office facilities. Certain of these noncancelable operating leases contain rental escalation clauses based on increases in the consumer price index. At the end of the lease obligations, renewal options may be exercised by the Company for up to an additional ten years.

Purchase obligations represent contractual service and other operating and marketing obligations of the Company.

Capital Resources

The Company, the Bank's holding company, had Tier 1 leverage, Tier 1 risk based and total risk-based capital ratios at December 31, 2003 of 14.2 percent, 15.6 percent and 18.2 percent, respectively, which represents \$158.4 million, \$150.7 million and \$128.1 million, respectively, of capital in excess of the amount required to be well capitalized for bank holding company regulatory purposes. Our trust preferred securities presently qualify as Tier 1 capital. As a result of the deconsolidation of our trust subsidiaries required by our adoption of FIN 46 as of December 31, 2003, the Federal Reserve Board is evaluating whether the deconsolidation will affect the qualification of the trust preferred securities as Tier 1 capital. See Note 10 to our consolidated financial statements included in Item 8 of this report.

The Bank had Tier 1 leverage, Tier 1 risk based and total risk-based capital ratios at December 31, 2003 of 13.2 percent, 14.3 percent and 15.6 percent, respectively, which represents \$133.6 million, \$124.7 million and \$83.5 million, respectively, of capital in excess of the amount required to be well capitalized for regulatory purposes. These ratios were 13.1%, 13.2% and 14.4% as of December 31, 2002, respectively.

Shareholders' equity increased to \$186.9 million at December 31, 2003 from \$156.7 million at December 31, 2002. The increase was primarily due to the retention of \$29.6 million of net income as retained earnings for the year and \$2.9 million received from the exercise of employee stock options, partially offset by the purchase of \$2.2 million of the Company's common stock currently held as treasury stock. There were no dividends declared or paid by us during 2003.

Table of Contents**Credit Risk Elements****Allowance for Loan Losses and Nonperforming Assets**

The following table provides certain information with respect to our total allowance for loan losses, including charge-offs, recoveries and selected ratios, for the periods indicated.

	As of and for the Years Ended December 31,				
	2003	2002	2001	2000	1999
	(dollars in thousands)				
Balance at beginning of year	\$ 33,009	\$ 26,650	\$ 27,186	\$ 19,895	\$ 16,811
Provision for loan losses	7,760	9,030	4,575	4,775	4,950
Addition due to purchase of the ICCMAC Trust				4,614	
Additions due to purchase of LHO and Asahi		2,048			
Charge offs:					
Real estate loans	(5,286)	(4,730)	(2,845)	(1,489)	(2,088)
Construction loans			(2,419)	(1,000)	
Film finance loans	(800)				
Franchise loans	(661)				
Commercial and other loans	(700)				
Total charge-offs	(7,447)	(4,730)	(5,264)	(2,489)	(2,088)
Recoveries:					
Real estate loans	14	11	153	391	222
Commercial and other loans	65				
Total recoveries	79	11	153	391	222
Net (charge-offs) recoveries	(7,368)	(4,719)	(5,111)	(2,098)	(1,866)
Balance at end of the year	\$ 33,401	\$ 33,009	\$ 26,650	\$ 27,186	\$ 19,895
Average loans outstanding during the year	\$ 1,415,812	\$ 1,305,902	\$ 1,295,097	\$ 1,147,602	\$ 925,059
Loans, net, at end of the year (1)	\$ 1,538,825	\$ 1,471,243	\$ 1,311,178	\$ 1,284,835	\$ 971,375
Selected Ratios:					
Net (charge-offs) recoveries to average loans outstanding	(0.52)%	(0.36)%	(0.39)%	(0.18)%	(0.20)%
Net (charge-offs) recoveries to loans, net (1)	(0.48)%	(0.32)%	(0.39)%	(0.16)%	(0.19)%
Allowance for loan losses to loans, net (1)	2.14%	2.31%	2.16%	2.12%	2.05%
Allowance for loan losses to nonaccrual loans	392.26%	555.61%	174.30%	149.85%	249.40%

(1) Loans, before allowance for loan losses and net of premium, deferred loan origination costs and deferred loan fees.

The allowance for loan losses increased to \$33.4 million or 2.14% of our total loan portfolio at December 31, 2003 from \$33.0 million or 2.31% of our total loan portfolio at December 31, 2002. The increase in the allowance was due primarily to the growth in the Bank's loan portfolio, which increased \$120.6 million in 2003. During 2003, we decreased our provision to \$7.8 million compared to \$9.0 million in 2002.

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

The current period provision for loan losses was recorded to provide reserves adequate to support the known and inherent risk of loss in the loan portfolio, and reflects the overall decline in total non-performing loans and other loans of concern from \$41.4 million at December 31, 2002 to \$39.8 million at December 31, 2003.

The allowance for loan losses increased to \$33.0 million or 2.31% of our total loan portfolio at December 31, 2002 from \$26.7 million or 2.03% of our total loan portfolio at December 31, 2001. During 2002, we increased our provision to \$9.0 million compared to \$4.6 million in 2001. The increases in the allowance was due primarily to the growth in our loan portfolio and the increase in our other loans of concern, which increased from \$21.5 million in 2001 to \$35.5 million in 2002.

The following table sets forth management's historical allocation of the allowance for loan losses by loan or contract category and the percentage of gross loans in each category to total gross loans at the dates indicated.

Loan Category:	December 31,				
	2003		2002		2001
	Allowance for loan losses	% of loans (1)	Allowance for loan losses	% of loans (1)	Allowance for loan losses
Secured by real estate	\$25,522	76%	\$28,348	86%	\$26,650
Film finance	4,354	13	2,961	9	
Franchise	3,185	10	1,490	5	
Commercial	340	1	210		
Total	\$33,401	100%	\$33,009	100%	\$26,650

[Additional columns below]

[Continued from above table, first column(s) repeated]

Loan Category:	December 31,				
	2001	2000		1999	
	% of loans (1)	Allowance for loan losses	% of loans (1)	Allowance for loan losses	% of loans (1)
Secured by real estate	100%	\$27,186	100%	\$19,895	100%
Film finance					
Franchise					
Commercial					
Total	100%	\$27,186	100%	\$19,895	100%

(1) Percentage represents the percent of gross loans in category to total gross loans.

Table of Contents

Management believes the allowance for loan losses accounting policy is critical to the portrayal and understanding of our financial condition and results of operations. As such, selection and application of this critical accounting policy involves judgments, estimates, and uncertainties that are susceptible to change. In the event that different assumptions or conditions were to prevail, and depending upon the severity of such changes, the possibility of materially different financial condition or results of operations is a reasonable likelihood.

Management periodically assesses the adequacy of the allowance for loan losses by reference to many factors that may be weighted differently at various times depending on prevailing conditions. These factors include, among other elements:

general portfolio trends relative to asset and portfolio size;

asset categories; potential credit and geographic concentrations; delinquency trends and nonaccrual loan levels; historical loss experience and risks associated with changes in economic, social and business conditions; and the underwriting standards in effect when the loan was made.

Accordingly, the calculation of the adequacy of the allowance for loan losses is not based solely on the level of nonperforming assets. Management believes that our allowance for loan losses as of December 31, 2003 was adequate to absorb the known and inherent risks of loss in the loan portfolio at that date. While management believes the estimates and assumptions used in its determination of the adequacy of the allowance are reasonable, there can be no assurance that such estimates and assumptions will not be proven incorrect in the future, or that the actual amount of future provisions will not exceed the amount of past provisions or that any increased provisions that may be required will not adversely impact our financial condition and results of operations. In addition, the determination of the amount of the Bank's allowance for loan losses is subject to review by bank regulators, as part of the routine examination process, which may result in the establishment of additional reserves based upon their judgment of information available to them at the time of their examination.

The following table sets forth the delinquency status of our loan portfolios at each of the dates indicated.

	December 31,					
	2003		2002		2001	
	Amount	Percent of Gross Portfolio	Amount	Percent of Gross Portfolio	Amount	Percent of Gross Portfolio
	(dollars in thousands)					
Period of Delinquency						
30 - 59 days	\$21,455	1.39%	\$17,500	1.19%	\$11,481	0.88%
60 - 89 days	882	0.06%	148	0.01%	7,954	0.61%
90 days or more	8,515	0.55%	5,941	0.40%	13,450	1.03%
Total loans delinquent	\$30,852	2.00%	\$23,589	1.61%	\$32,885	2.52%



The increase in total delinquent loans in 2003 was due primarily to an increase of \$3.0 million of past due film finance loans, a \$799,000 increase in past due franchise loans and a \$577,000 increase of past due loans held in trust, partially offset by a \$1.8 million decrease in past due commercial real estate loans.

The Company has established a policy that all loans greater than \$1.5 million are reviewed annually. This review usually involves obtaining updated information about the collateral and source of repayment. In addition, independent outside consultants periodically review the Bank's loan portfolio and report findings to management and the audit committee of the board of directors. Loans considered to warrant special attention are presented to the review and reserve committee, which meets at least monthly to review the status of classified loans, consider new classifications or declassifications, determine the need for and amount of any charge offs, and recommend to our executive committee of the board of directors the level of allowance for loan losses to be maintained. If management believes that the collection of the full amount of principal is unlikely and the value of the collateral securing the obligation is insufficient, steps are generally taken to protect and liquidate the collateral. Losses resulting from the difference between the loan balance and the fair market value of the collateral are recognized by a partial charge-off of the loan balance to the collateral.

Table of Contents

fair market value. While real property collateral is held for sale, it is subject to periodic evaluation and/or appraisal. If an evaluation or appraisal indicates that the property will ultimately sell for less than our recorded value plus costs of disposition, the loss is recognized by a charge to allowance for loan losses on other real estate owned.

Loans are placed on nonaccrual status when they become 90 days or more contractually delinquent, or earlier if the collection of interest is considered by management to be doubtful, unless the loan is considered well secured and in the process of collection. Subsequent cash collections on nonaccrual loans are either recognized as interest income on a cash basis, if the loan is well secured and in management's judgment the net book value is fully collectible, or recorded entirely as a reduction of principal.

The following table sets forth our nonperforming assets by category and troubled debt restructurings as of the dates indicated:

	December 31,				
	2003	2002	2001	2000	1999
	(dollars in thousands)				
Nonaccrual loans:(1)					
Real estate	\$ 4,686	\$ 3,913	\$ 13,690	\$ 9,430	\$ 7,977
Construction			1,600	8,712	
Franchise	799	1,986			
Film finance	3,030				
Other real estate owned, net	7,048	12,593	13,741	2,250	1,041
Total nonperforming assets	15,563	18,492	29,031	20,392	9,018
Accruing loans past-due 90 days or more with respect to principal or interest				9,765	
Performing troubled debt restructurings	4,709	7,858	3,752	3,002	13,996
	\$ 20,272	\$ 26,350	\$ 32,783	\$ 33,159	\$ 23,014
Nonaccrual loans to total gross loans and real estate loans in trust	0.55%	0.36%	1.17%	1.42%	0.82%
Allowance for loan losses to nonaccrual loans	392.26%	555.61%	174.30%	149.85%	249.40%
Nonperforming assets to total assets	0.86%	1.08%	1.92%	1.44%	0.81%

(1) Includes three loans with a net book balance of \$3.8 million that were nonperforming troubled debt restructurings in 2003 and one loan with net book balance of \$1.4 million that was a nonperforming troubled debt restructuring in 2000.

Gross interest income that would have been recorded on nonaccrual loans had they been current in accordance with original terms was \$608,000 and \$941,000 for the years ended December 31, 2003 and 2002 respectively. The amount of interest income on such nonaccrual loans included in net income for the years ended December 31, 2003 and 2002 was \$290,000 and \$244,000, respectively.

Our nonaccrual loans totaled \$8.5 million at December 31, 2003. Two of these loans had an outstanding balance greater than \$1.0 million.

In 2003, \$9.6 million of new other real estate owned was acquired, \$14.2 million of other real estate owned was sold, and a provision of \$870,000 was recorded, resulting in net other real estate owned at December 31, 2003 of \$7.0 million. Other real estate owned at December 31, 2003 consisted of three properties with an average balance of approximately \$2.3 million. The other real estate owned property with the largest net book balance totaled \$4.8 million.

In addition to the above, management has concerns as to the borrowers' ability to comply with present repayment terms on \$31.3 million of other loans of concern as of December 31, 2003. See Item 1. Business Nonperforming Assets and Other Loans of Concern.

Table of Contents**Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

We realize income principally from the differential or spread between the interest earned on loans, investments and other interest-earning assets and the interest paid on deposits and borrowings. Loan volumes and yields, as well as the volume of and rates on investments, deposits and borrowings, are affected by market interest rates. Additionally, because of the terms and conditions of many of our loan agreements and deposit accounts, a change in interest rates could also affect the duration of the loan portfolio and/or the deposit base, which could alter our sensitivity to future changes in interest rates.

Interest rate risk management focuses on maintaining consistent growth in net interest income within board-approved policy limits while taking into consideration, among other factors, our overall credit, operating income, operating cost and capital profile. The asset/liability management committee, which includes senior management representatives and reports to the Board of Directors, monitors and manages interest rate risk to maintain an acceptable level of change in net interest income as a result of changes in interest rates. See Item 1. Business Nonperforming Assets and Other Loans of Concern .

In evaluating our exposure to changes in interest rates, certain risks inherent in the method of analysis presented in the following table must be considered. For example, although certain assets and liabilities may have similar maturities or periods to repricing, they may react in different degrees and at different times to changes in market rates. Additionally, loan prepayments and early withdrawals of time certificates could cause interest sensitivities to vary from those that appear in the following table. Further, certain assets, such as variable rate real estate loans, have features that restrict changes in interest rates on a short-term basis and over the life of the asset. The majority of our variable rate real estate loans may not adjust downward below their initial rate, with increases generally limited to maximum adjustments of 2% per year and up to 5% over the life of the loan. These loans may also be subject to prepayment penalties. At December 31, 2003, 83.4% of our variable rate loan portfolio would not adjust downward below the initial interest rate with the weighted-average minimum interest rate on this portfolio being 6.87% and 77.4% of the total loans outstanding had a lifetime interest rate cap, with the weighted-average lifetime interest rate cap on this portfolio being 9.28%. The anticipated effects of these various factors are considered by management in implementing interest rate risk management activities.

We use an internal earnings simulation model as a tool to identify and manage our interest rate risk profile. The model is based on projected cash flows and repricing characteristics for all financial instruments and incorporates market-based assumptions regarding the impact of changing interest rates on current volumes of applicable financial instruments, considering applicable interest rate floors and caps and prepayment penalties associated with each financial instrument. These assumptions are inherently uncertain and, as a result, the model cannot precisely measure net interest income or precisely predict the impact of changes in interest rates on net interest income. Actual results will differ from simulated results due to timing, magnitude and frequency of interest rate changes as well as changes in market conditions and management strategies.

The following table shows our estimated earnings sensitivity profile as of December 31, 2003:

Changes in Interest rates (Basis Points)	Percentage Change in Net Interest Income (12 Months)
+ 200 Over One Year	1.67%
+ 100 Over One Year	- 0.20%
- 100 Over One Year	1.92%
- 200 Over One Year	N/A

Because of the low level of current market interest rates, the above analysis was not performed for an interest rate decrease greater than 100 basis points.

Another tool used to identify and manage our interest rate risk profile is the static gap analysis. Interest sensitivity gap analysis measures the difference between the assets and liabilities repricing or maturing within specific time periods. Although our cumulative GAP position indicates an asset-sensitive position, our loan portfolio has reached floor interest rates in excess of current market rates to such an extent that a 150 basis point increase in rates does not cause our assets to reprice. Our liabilities within the cumulative GAP period reprice upward to market rates under this scenario causing compression of net interest income. In a declining rate environment, our liabilities will continue to reprice downward, while our loan portfolio remains at its floor rates, creating an increase in net interest income.

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Table of Contents

The following table presents an estimate of our static GAP analysis as of December 31, 2003.

	Maturing or Repricing in					Total
	3 months or less	After 3 Months But Within 1 year	After 1 Year But Within 5 Years	After 5 Years	Non-Interest Sensitive	
(dollars in thousands)						
Assets						
Loans (1)	\$ 793,130	\$564,346	\$ 109,151	\$ 1,795	\$	\$1,468,422
Real estate loans held in trust(2)	32,278	22,164	15,956	5		70,403
Cash and cash equivalents	174,046				4,272	178,318
Investment securities available for sale	8,183	34,306	9,880	18,690		71,059
Noninterest-earning assets less allowance for loan losses and unearned fees					30,013	30,013
Total assets	\$1,007,637	\$620,816	\$ 134,987	\$ 20,490	\$ 34,285	\$1,818,215
Liabilities and Shareholders Equity						
Time certificates under \$100,000	\$ 129,702	\$315,809	\$ 118,696	\$	\$	\$ 564,207
Time certificates \$100,000 and more	96,922	196,284	85,507			378,713
Money market and passbook accounts	109,803	38,196	8,506			156,505
Demand deposit accounts	47,592					47,592
FHLB advances	299,900	16,000	36,705	9,530		362,135
Collateralized mortgage obligations	15,868					15,868
Other liabilities					19,696	19,696
Junior subordinated debentures	57,561			29,039		86,600
Shareholders equity					186,899	186,899
Total liabilities and shareholders equity	\$ 757,348	\$566,289	\$ 249,414	\$ 38,569	\$ 206,595	\$1,818,215
Net repricing assets over (under) repricing liabilities equals interest rate sensitivity GAP	\$ 250,289	\$ 54,527	\$(114,427)	\$ (18,079)	\$(172,310)	
Cumulative interest rate sensitivity GAP	\$ 250,289	\$304,816	\$ 190,389	\$172,310	\$	
Cumulative GAP as a percentage of total assets	13.77%	16.76%	10.47%	9.48%	0.0%	

(1) Adjustable rate loans consist principally of real estate secured loans with a maximum term of 30 years. Approximately 65% of these loans are generally adjustable quarterly based on changes in various indexes, subject generally to a maximum increase of 2% annually and up to 5% over the life of the loan. Approximately 17% of these loans are fixed for an initial period of two to five years from origination, and then are adjustable quarterly based on changes in various indexes. Nonaccrual loans of approximately \$7.7 million are assumed to reprice after five years.

*(2) Nonaccrual
loans of
approximately
\$809,000 are
assumed to
reprice after
five years.*

Table of Contents

Item 8. Financial Statements and Supplementary Data

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

	Page
Report of Independent Auditors	38
Report of Predecessor Independent Public Accountants	39
Consolidated Balance Sheets as of December 31, 2003 and 2002	40
Consolidated Statements of Income for the Years Ended December 31, 2003, 2002 and 2001	41
Consolidated Statements of Changes in Shareholders' Equity and Comprehensive Income for the Years Ended December 31, 2003, 2002 and 2001	42
Consolidated Statements of Cash Flows for the Years Ended December 31, 2003, 2002 and 2001	43
Notes to Consolidated Financial Statements	44

Table of Contents

REPORT OF INDEPENDENT AUDITORS

To the Shareholders and the Board of Directors of
ITLA Capital Corporation:

We have audited the accompanying consolidated balance sheets of ITLA Capital Corporation and subsidiaries (the Company), a Delaware corporation, as of December 31, 2003 and 2002, and the related consolidated statements of income, changes in shareholders' equity and comprehensive income, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of ITLA Capital Corporation and subsidiaries at December 31, 2003 and 2002, and the consolidated results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States.

As are further described in Note 1 to the consolidated financial statements, at December 31, 2003 the Company adopted FASB Interpretation No. (FIN) 46, Consolidation of Variable Interest Entities, as revised, which required the deconsolidation of its trust subsidiaries that had issued its mandatorily redeemable preferred securities and to which the Company issued its junior subordinated debentures.

/s/ Ernst & Young LLP

Los Angeles, California
January 30, 2004

Table of Contents

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Shareholders and the Board of Directors of
ITLA Capital Corporation:

We have audited the accompanying consolidated balance sheets of ITLA Capital Corporation and subsidiaries (the Company), a Delaware corporation, as of December 31, 2001 and 2000, and the related consolidated statements of income, changes in shareholders equity and cash flows for each of the three years in the period ended December 31, 2001. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of ITLA Capital Corporation and subsidiaries as of December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States.

/s/ Arthur Andersen LLP

Los Angeles, California
January 25, 2002

This is a copy of the audit report previously issued by Arthur Andersen LLP in connection with ITLA Capital Corporation s filing on Form 10-K for the year ended December 31, 2001. Arthur Andersen LLP has not reissued this report in connection with this filing on Form 10-K.

Table of Contents**ITLA CAPITAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS**

	December 31,	
	2003	2002
	(in thousands except share amounts)	
Assets		
Cash and cash equivalents	\$ 178,318	\$ 160,848
Investment securities available for sale, at fair value	53,093	54,677
Stock in Federal Home Loan Bank	17,966	16,934
Loans, net (net of allowance for loan losses of \$31,573 and \$31,081 in 2003 and 2002, respectively)	1,436,849	1,316,298
Real estate loans held in trust, net (net of allowance for loan losses of \$1,828 and \$1,928 in 2003 and 2002, respectively)	68,575	121,936
Interest receivable	8,958	9,158
Other real estate owned, net	7,048	12,593
Premises and equipment, net	5,766	4,197
Deferred income taxes	11,609	13,822
Goodwill	3,118	3,118
Other assets	26,915	8,384
	<u> </u>	<u> </u>
Total assets	\$1,818,215	\$1,721,965
	<u> </u>	<u> </u>
Liabilities and Shareholders' Equity		
Liabilities:		
Deposit accounts	\$1,147,017	\$1,065,911
Federal Home Loan Bank advances	362,135	338,685
Collateralized mortgage obligations	15,868	69,077
Accounts payable and other liabilities	19,696	10,006
Junior subordinated debentures	86,600	—
	<u> </u>	<u> </u>
Total liabilities	1,631,316	1,483,679
	<u> </u>	<u> </u>
Commitments and contingencies (note 16)		
Guaranteed preferred beneficial interests in the Company's junior subordinated deferrable interest debentures		81,595
Shareholders' equity:		
Preferred stock, 5,000,000 shares authorized, none issued		
Contributed capital—common stock, \$.01 par value; 20,000,000 shares authorized, 8,447,294 and 8,226,414 issued in 2003 and 2002, respectively	61,704	58,841
Retained earnings	165,407	135,773
Accumulated other comprehensive income, net	155	435
	<u> </u>	<u> </u>
	227,266	195,049
Less treasury stock, at cost—2,475,689 and 2,447,656 shares in 2003 and 2002, respectively	(40,367)	(38,358)
	<u> </u>	<u> </u>
Total shareholders' equity	186,899	156,691
	<u> </u>	<u> </u>
Total liabilities and shareholders' equity	\$1,818,215	\$1,721,965
	<u> </u>	<u> </u>

See accompanying notes to the consolidated financial statements.

Table of Contents**ITLA CAPITAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME**

	Years Ended December 31,		
	2003	2002	2001
	(in thousands except per share amounts)		
Interest income:			
Loans receivable, including fees	\$ 104,598	\$ 96,894	\$ 104,949
Real estate loans held in trust	5,980	10,239	14,954
Cash and investment securities	5,399	3,475	3,192
Total interest income	115,977	110,608	123,095
Interest expense:			
Deposit accounts	24,616	29,349	52,864
Federal Home Loan Bank advances	5,175	5,672	4,790
Collateralized mortgage obligations	1,076	2,301	6,209
Total interest expense	30,867	37,322	63,863
Net interest income before provision for loan losses	85,110	73,286	59,232
Provision for loan losses	7,760	9,030	4,575
Net interest income after provision for loan losses	77,350	64,256	54,657
Non-interest income:			
Premium on sale of loans, net	8,983		
Late and collection fees	252	201	274
Other	6,005	172	785
Total non-interest income	15,240	373	1,059
Non-interest expense:			
Compensation and benefits	18,870	13,954	11,778
Occupancy and equipment	4,839	3,165	2,968
Other	13,006	9,913	8,072
Total general and administrative	36,715	27,032	22,818
Real estate owned expense, net	382	632	136
Provision for losses on other real estate owned	870	796	269
Gain on sale of other real estate owned, net	(40)	(105)	(18)
Total real estate owned expense, net	1,212	1,323	387
Total non-interest expense	37,927	28,355	23,205
Income before provision for income taxes and minority interest in income of subsidiary	54,663	36,274	32,511
Minority interest in income of subsidiary	6,083	3,481	2,967
Income before provision for income taxes	48,580	32,793	29,544

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Provision for income taxes	<u>18,946</u>	<u>12,788</u>	<u>11,393</u>
NET INCOME	<u>\$ 29,634</u>	<u>\$ 20,005</u>	<u>\$ 18,151</u>
BASIC EARNINGS PER SHARE	<u>\$ 4.91</u>	<u>\$ 3.35</u>	<u>\$ 2.82</u>
DILUTED EARNINGS PER SHARE	<u>\$ 4.55</u>	<u>\$ 3.16</u>	<u>\$ 2.72</u>

See accompanying notes to the consolidated financial statements.

Table of Contents**ITLA CAPITAL CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME**

	Common Stock Number of shares		
	Gross Shares Issued and Outstanding	Treasury Shares	Net Shares Issued and Outstanding
	(in thousands except share amounts)		
Balance at January 1, 2001	8,206,749	(1,546,336)	6,660,413
Issuance of common stock - employee stock options	6,000		6,000
Earned compensation from Supplemental Executive Retirement Plan / Recognition and Retention Plan, net		1,980	1,980
Common stock repurchased		(809,700)	(809,700)
Net income			
Total comprehensive income			
Balance at December 31, 2001	8,212,749	(2,354,056)	5,858,693
Issuance of common stock-employee stock options	13,665		13,665
Earned compensation from Supplemental Executive Retirement Plan / Recognition and Retention Plan, net			
Common stock repurchased		(93,600)	(93,600)
Net income			
Total comprehensive income			
Balance at December 31, 2002	8,226,414	(2,447,656)	5,778,758
Issuance of common stock- employee stock options	220,880		220,880
Earned compensation from Supplemental Executive Retirement Plan / Recognition and Retention Plan, net		24,919	24,919
Common stock repurchased		(52,952)	(52,952)
Net income			
Total comprehensive income			
Balance at December 31, 2003	8,447,294	(2,475,689)	5,971,605

[Additional columns below]

[Continued from above table, first column(s) repeated]

Shareholders' Equity

Contributed Capital	Accumulated
---------------------	-------------

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

	Share Capital	Earned Compensation	Total Contributed Capital	Retained Earnings	Other Comprehensive Income (loss)	Treasury Stock, At Cost	Total
(in thousands except share amounts)							
Balance at January 1, 2001	\$56,495	\$ 625	\$57,120	\$ 97,617	\$ 91	\$(21,274)	\$ 133,554
Issuance of common stock - employee stock options	74		74				74
Earned compensation from Supplemental Executive Retirement Plan /Recognition and Retention Plan, net		989	989			18	1,007
Common stock repurchased						(14,759)	(14,759)
Net income				18,151			18,151
Total comprehensive income					(98)		(98)
Balance at December 31, 2001	56,569	1,614	58,183	115,768	(7)	(36,015)	137,929
Issuance of common stock-employee stock options	184		184				184
Earned compensation from Supplemental Executive Retirement Plan / Recognition and Retention Plan, net		474	474				474
Common stock repurchased						(2,343)	(2,343)
Net income				20,005			20,005
Total comprehensive income					442		442
Balance at December 31, 2002	56,753	2,088	58,841	135,773	435	(38,358)	156,691
Issuance of common stock- employee stock options	2,897		2,897				2,897
Earned compensation from Supplemental Executive Retirement Plan / Recognition and Retention Plan, net		(34)	(34)			224	190
Common stock repurchased						(2,233)	(2,233)
Net income				29,634			29,634
Total comprehensive income					(280)		(280)
Balance at December 31, 2003	\$59,650	\$ 2,054	\$61,704	\$ 165,407	\$ 155	\$(40,367)	\$ 186,899

[Additional columns below]

[Continued from above table, first column(s) repeated]

Comprehensive Income			
Net Income	Unrealized Gain (loss) on securities, net of tax	Reclassification of realized gains previously recognized in comprehensive	Total Comprehensive Income

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

			income, net of tax	
(in thousands except share amounts)				
Balance at January 1, 2001				
Issuance of common stock - employee stock options				
Earned compensation from Supplemental Executive Retirement Plan / Recognition and Retention Plan, net				
Common stock repurchased				
Net income				
Total comprehensive income	\$ 18,151	\$ (98)	\$	\$ 18,053
Balance at December 31, 2001				
Issuance of common stock-employee stock options				
Earned compensation from Supplemental Executive Retirement Plan / Recognition and Retention Plan, net				
Common stock repurchased				
Net income				
Total comprehensive income	20,005	442	\$	20,447
Balance at December 31, 2002				
Issuance of common stock- employee stock options				
Earned compensation from Supplemental Executive Retirement Plan / Recognition and Retention Plan, net				
Common stock repurchased				
Net income				
Total comprehensive income	\$ 29,634	\$ (280)	\$	\$ 29,354
Balance at December 31, 2003				

See accompanying notes to the consolidated financial statements.

Table of Contents**ITLA CAPITAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS**

	Years Ended December 31,		
	2003	2002	2001
	(in thousands)		
Cash Flows From Operating Activities:			
Net Income	\$ 29,634	\$ 20,005	\$ 18,151
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization of premises and equipment	1,722	946	836
Amortization of premium on purchased loans	2,136	1,859	3,143
Amortization of original issue discount and deferred debt issuance costs on CMOs	328	168	294
Amortization of deferred loan origination fees, net of costs	(2,390)	(1,688)	(1,333)
Provision for loan losses	7,760	9,030	4,575
Provision for losses on other real estate owned	870	796	269
Deferred income tax expense (benefit)	2,399	(2,255)	(546)
Other, net	216	(105)	(18)
Decrease in interest receivable	200	1,986	677
(Increase) decrease in other assets	(13,795)	363	462
Increase (decrease) in accounts payable and other liabilities	9,690	(368)	(654)
	<u>38,770</u>	<u>30,737</u>	<u>25,856</u>
Cash Flows From Investing Activities:			
Proceeds from securitization and sale of real estate loans		98,155	
Purchases of investment securities available for sale	(55,395)	(102,462)	(45,400)
Proceeds from the maturity and calls of investment securities available for sale	55,894	78,705	62,260
Purchase of stock in Federal Home Loan Bank	(479)	(3,470)	(9,160)
Purchase of loans	(54,053)	(90,909)	(207,400)
(Increase) decrease in loans, net	(76,100)	(84,889)	108,493
Repayment of real estate loans held in trust	51,946	38,896	47,927
Proceeds from sale of real estate loans			755
Proceeds from sale of other real estate owned	8,226	3,972	5,687
Cash paid for capital expenditures	(3,291)	(2,859)	(752)
Cash paid to acquire LHO, net		(93,042)	
Cash paid to acquire Asahi Bank of California, net		(14,872)	
Other, net			(331)
	<u>(73,252)</u>	<u>(172,775)</u>	<u>(37,921)</u>
Cash Flows From Financing Activities:			
Proceeds from exercise of employee stock options	2,897	184	74
Cash paid to acquire treasury stock	(2,233)	(2,343)	(14,759)
Repayment of Asahi repurchase agreement, net		(14,693)	
Proceeds from issuance of trust preferred securities		53,348	14,549
Principal payments on collateralized mortgage obligations	(53,268)	(40,739)	(52,498)
Increase (decrease) in deposit accounts	81,106	103,488	(62,045)
Net proceeds from short-term borrowings from the Federal Home Loan Bank	64,000	9,700	124,800
Proceeds from long-term borrowings from the Federal Home Loan Bank	16,000	109,700	75,235
	<u>(56,550)</u>	<u>(50,000)</u>	<u>(10,000)</u>

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Repayments of long-term borrowings from the Federal Home Loan
Bank

	51,952	168,645	75,356
Net cash provided by financing activities			
Net increase in cash and cash equivalents	17,470	26,607	63,291
Cash and cash equivalents, beginning of period	160,848	134,241	70,950
	\$ 178,318	\$ 160,848	\$ 134,241
Supplemental Cash Flow Information:			
Cash paid during the period for interest	\$ 31,181	\$ 36,753	\$ 65,073
Cash paid during the period for income taxes	\$ 19,965	\$ 15,247	\$ 9,750
Non-cash Investing Transactions:			
Loans transferred to other real estate owned	\$ 9,609	\$ 3,515	\$ 16,961
Loans to facilitate the sale of other real estate owned	\$ 6,098	\$ 2,860	\$ 2,050

See accompanying notes to the consolidated financial statements.

Table of Contents

ITLA CAPITAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2003, 2002, AND 2001

NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization - ITLA Capital Corporation and subsidiaries (ITLA Capital or the Company) is primarily engaged in the origination of real estate loans secured by income producing real estate and, to a lesser extent, the origination of franchise, film finance, tax refund anticipation, and private label commercial revolving credit loans. Through our principal operating subsidiary, Imperial Capital Bank (Imperial or the Bank), the Company accepts deposits insured by the Federal Deposit Insurance Corporation (FDIC) which are used primarily to fund the investment in variable rate loans. The Company also holds 100 percent of the equity and certain collateralized mortgage obligations (CMOs) of the ICCMAC Multifamily and Commercial Trust 1999-1 (the ICCMAC Trust), through our Imperial Capital Real Estate Investment Trust (Imperial Capital REIT) subsidiary.

In 2002 we formed ITLA Capital Statutory Trust III (Trust III), ITLA Capital Statutory Trust IV (Trust IV), and ITLA Capital Statutory Trust V (Trust V), and in 2001 and 2000, we formed ITLA Capital Statutory Trust II (Trust II) and ITLA Capital Statutory Trust I (Trust I), respectively. Collectively, these trusts are referred to as the Trusts. The Trusts were established solely for the purpose of issuing Guaranteed Preferred Beneficial Interests in the Company's Junior Subordinated Deferrable Interest Debentures (the Trust Preferred securities). As discussed further in the new accounting pronouncement section below, and in Note 10 Junior subordinated debentures, the Company deconsolidated the Trusts as of December 31, 2003. As a result, the Company recorded the \$86.6 million of underlying debentures issued by the Company to the Trusts as Junior subordinated debentures and \$2.6 million of the Company's investment in the Trusts and \$2.1 million of deferred debt issuance costs as Other assets in the consolidated balance sheet at December 31, 2003. The entries recorded in connection with the deconsolidation of the Trusts are non-cash investing transactions for cash flow purposes.

During 2002, the Company formed ITLA Mortgage Loan Securitization 2002-1, LLC, a limited liability company to issue certain asset-backed notes in connection with the securitization of the Company's performing residential loan portfolio.

In November 2002, the Company entered into a strategic business relationship with various subsidiaries of Household International, Inc. (Household) relating to certain tax refund products. In connection with this relationship, the Bank originates tax refund anticipation loans and sells Household a non-recourse participation interest representing substantially all of the outstanding loan balance. Under the agreement, Household supports the Bank's credit administration, compliance, treasury, and accounting functions with a range of services relating to the administration of this program. Household also services the loans on behalf of the Bank. Substantially all of the tax refund lending volume is generated during the first quarter of the year. The tax refund agreement is for a four-year term, with substantial break-up fees that apply in the event that Household terminates the agreement during the first two years of the agreement. The Bank was affirmed by Household in November 2003, as its strategic lending partner for the 2004 tax season.

The Company also entered into an agreement in December 2002 with Household pursuant to which the Bank originates private label commercial revolving credit loans to small businesses. This agreement is for a two-year term. These loans are used primarily to fund purchases from major retailers. Pursuant to this agreement, the Bank sells Household a non-recourse participation interest representing substantially all of the outstanding loan balance.

As of December 31, 2003 and 2002, the Bank had no tax refund anticipation loans (RAL) outstanding and \$5.8 million and \$4.2 million, respectively, of private label commercial revolving loans outstanding. Fee income earned in connection with the RAL program, consisted of approximately \$9.0 million of net premiums on the sale of RAL loans and \$4.6 million of processing and administrative fees. Because the RAL program relates to the filing of income tax returns, transaction activity was concentrated during the tax season. This resulted in the Company earning substantially all of its RAL program income in the first quarter of the year.

Imperial began operating as a California industrial bank in 1974, and became a publicly traded company in October 1995, when its shares were sold in an initial public offering. Imperial operates six retail branches in California and one branch in Nevada, along with six lending offices located in California, Nevada, Arizona, Texas, Washington, and Georgia. From its formation in 1974 until December 31, 1999, Imperial operated under the name Imperial Thrift and Loan Association. Effective January 1, 2000, Imperial changed its name to Imperial Capital Bank.

Table of Contents

In December 2002, the Bank received regulatory approval to convert to a California state chartered commercial bank from a California industrial bank. In addition, ITLA Capital was approved by the Federal Reserve Bank to become a bank holding company. The Bank began operating as a commercial bank and ITLA Capital became a bank holding company in January 2003.

Financial Statement Presentation The accounting and reporting policies of the Company conform to accounting principles generally accepted in the United States (GAAP) and to prevailing practices within the financial services industry. The consolidated financial statements include the accounts of the Company, its wholly-owned subsidiaries, and variable interest entities for which the Company is the primary beneficiary. All material intercompany transactions and balances have been eliminated. Certain amounts in prior periods have been reclassified to conform to the presentation in the current period. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents We consider all highly liquid investments with original maturities of three months or less to be cash equivalents.

Investment Securities Investment securities available for sale are carried at fair value with unrealized gains or losses reported net of taxes as a component of other comprehensive income (loss) until realized. Realized gains and losses are determined using the specific identification method.

Loans Loans, which include real estate loans, franchise loans, film finance loans, tax refund anticipation loans, commercial revolving credit loans and real estate loans held in trust, are generally carried at principal amounts outstanding plus purchase premiums, less charge-offs, net deferred loan origination fees and other unearned income. Deferred loan origination fees and other unearned income include deferred unamortized fees net of direct incremental loan origination costs. Interest income is accrued as earned. Net purchase premiums or discounts and deferred loan origination fees are amortized or accreted into interest income using the interest method. Premium on the sale of loans consists entirely of income earned in connection with the sale of refund anticipation loans to Household and is recognized as income at the time the loans are purchased by Household.

Loans are placed on nonaccrual status when they become 90 days or more contractually delinquent or earlier if the collection of interest is considered by management to be unlikely. When a loan is placed on nonaccrual status, all previously accrued but uncollected interest is reversed against current period operating results. Subsequent cash collections on nonaccrual loans are either recognized as interest income on a cash basis if the loan is well secured and in management's judgment the net book value is fully collectible, or recorded as a reduction of principal.

Loans are considered impaired when, based upon current information and events, it is probable that the Company will be unable to collect all principal and interest amounts due according to the original contractual terms of the loan agreement on a timely basis. The Company evaluates impairment on a loan-by-loan basis. Once a loan is determined to be impaired, the impairment is measured based on the present value of the expected future cash flows discounted at the loan's effective interest rate or by using the loan's most recent market price or the fair value of the collateral if the loan is collateral dependent.

When the measurement of an impaired loan is less than the recorded amount of the loan, a valuation allowance is established by recording a charge to the provision for loan losses. Subsequent increases or decreases in the valuation allowance for impaired loans are recorded by adjusting the existing valuation allowance for the impaired loan with a corresponding charge or credit to the provision for loan losses.

Our policy for recognizing interest income on impaired loans is the same as that for nonaccrual loans.

Allowance for Loan Losses - We maintain an allowance for loan losses at a level considered adequate to cover probable losses on loans. In evaluating the adequacy of the allowance for loan losses, management estimates the amount of the loss for each loan that has been identified as having more than standard credit risk. Those estimates give consideration to, among other factors, economic conditions, estimated real estate collateral value and cash flow, and the financial strength and commitment of the borrower or guarantors, where appropriate. Additionally, an estimate for loan loss is calculated for the remaining portion of the portfolio giving consideration to the Company's historical loss experience in the portfolio, adjusted, as appropriate, for the estimated effects of current economic conditions and changes in the composition of the loan portfolio over time. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance, or portion thereof, has been confirmed.

Table of Contents

Other Real Estate Owned Other real estate owned (OREO) represents real estate acquired through or in lieu of foreclosure. OREO is held for sale and is initially recorded at fair value less estimated costs of disposition at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of cost or estimated fair value less costs of disposition. The net operating results from OREO are recognized as non-interest expense.

Premises and Equipment Premises and equipment are recorded at cost, less accumulated depreciation and amortization. Depreciation is calculated on the straight-line method over the estimated useful lives of the assets ranging from three to twelve years. Amortization of leasehold improvements is calculated on the straight-line method over the shorter of the estimated useful lives of the assets or the corresponding lease term.

Goodwill The Company adopted Statement of Financial Accounting Standards (SFAS) No. 142, Goodwill and Other Intangible Assets , on January 1, 2002. The adoption of SFAS No. 142 ceased the amortization of goodwill and requires an annual assessment for impairment by applying a fair-value-based test. In connection with acquisitions discussed in Note 2, the Company recognized approximately \$3.1 million of goodwill. In accordance with SFAS No. 142, the Company assesses the goodwill for impairment on an annual basis, or on an interim basis if events or circumstances indicate the fair value of the goodwill has decreased below its carrying value. During 2003 and 2002, the Company evaluated its goodwill, and determined that no impairment was required.

Income Taxes Provision for income taxes is the amount of estimated tax due reported on our tax returns and the change in the amount of deferred tax assets and liabilities. Deferred income taxes represent the estimated net income tax expense payable (or benefits receivable) for temporary differences between the carrying amounts for financial reporting purposes and the amounts used for tax purposes.

Earnings Per Share - Earnings per share (EPS) for all periods presented in the consolidated statements of income are computed in accordance with the provisions of SFAS No. 128 - Earnings Per Share , and are based on the weighted-average number of shares outstanding during each year. Basic EPS excludes dilution and is computed by dividing income available to common shareholders by the weighted-average number of common shares outstanding during the period. Diluted EPS includes the effect of common stock equivalents of the Company, which include only shares issuable on the exercise of outstanding options. A reconciliation of the computation of Basic EPS and Diluted EPS is presented in Note 18 Earnings Per Share.

Stock-Based Compensation The Company s stock-based compensation plan is accounted for in accordance with Accounting Principles Board (APB) Opinion No. 25 Accounting for Stock Issued to Employees . Under APB Opinion No. 25, no compensation expense is recognized for a stock option grant if the exercise price of the stock option at measurement date is equal to or greater than the fair market value of the common stock on the date of grant. The Company applies SFAS No. 123 for disclosure purposes only. SFAS No. 123 disclosures include pro forma net income and earning per share as if the fair value-based method of accounting had been used. If compensation had been determined based on SFAS No. 123, the Company s pro forma net income and pro forma per share data would be as follows:

	For the Year Ended December 31,		
	2003	2002	2001
	(in thousands, except per share data)		
Net income, as reported	\$29,634	\$20,005	\$18,151
Less: Stock-based employee compensation expense determined under the fair value method, net of tax	(1,440)	(1,076)	
Pro forma net income	\$28,194	\$18,929	\$18,151
Earnings per share:			
Basic as reported	\$ 4.91	\$ 3.35	\$ 2.82
Basic pro forma	\$ 4.68	\$ 3.17	\$ 2.82
Diluted as reported	\$ 4.55	\$ 3.16	\$ 2.72
Diluted pro forma	\$ 4.33	\$ 2.99	\$ 2.72

Comprehensive Income - Comprehensive income is displayed in the Consolidated Statements of Changes in Shareholders Equity and Comprehensive Income and consists entirely of the change in net unrealized holding gain or loss on securities classified as available for sale, net of the related income tax effect.

Table of Contents

New Accounting Pronouncements In November 2002, Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 45 (FIN 45), Guarantor s Accounting and Disclosure Requirement for Guarantees, Including Indirect Guarantees of Indebtedness of Others. FIN 45 elaborates on the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. It also clarifies that a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. The initial recognition and measurement provisions for FIN 45 are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. The disclosure requirements of FIN 45 are effective for financial statements of interim or annual periods ending after December 15, 2002, and were included in the Company s financial statements for the year ended December 31, 2003. Implementation of the provisions of FIN 45 did not have a material impact on the Company s financial statements.

In January 2003, FASB issued FASB Interpretation No. 46 (FIN 46), Consolidation of Variable Interest Entities. FIN 46 establishes the criteria used to identify variable interest entities and to determine whether or not to consolidate a variable interest entity. The Company adopted FIN 46 at December 31, 2003. In accordance therewith, the Company deconsolidated the Trusts. The result was to recognize investments in the Trusts in other assets, and to report the amount of subordinated debentures issued by the Company to the Trusts in the liability section of the Company s consolidated balance sheet. In addition, beginning January 1, 2004, the Company will recognize the interest expense on the subordinated debentures in the consolidated statements of income. Prior to FIN 46, the Company consolidated the Trusts and reported trust preferred securities in the mezzanine section of the Company s consolidated balance sheets and recognized the proportionate share of income attributable to the preferred shareholders as minority interest in income of subsidiary in the consolidated statements of income. This interpretation was effective immediately for variable interest entities created after January 31, 2003 and was initially to be effective for variable interest entities acquired prior to February 1, 2003, in the quarter ended September 30, 2003. Effective October 9, 2003, the FASB agreed to defer the effective date of FIN 46 for variable interests held by public companies in all entities that were acquired prior to February 1, 2003. The deferral required public companies to adopt the provisions of FIN 46 for periods ended after December 15, 2003. Adoption of FIN 46, as revised, did not have a material impact on the results of operations or financial position, but will affect net interest income. As a result of the adoption of FIN 46 at December 31, 2003, financial information prior to the adoption has not been restated.

On May 15, 2003, FASB issued SFAS No. 150, Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity. SFAS No. 150 modifies the accounting for certain financial instruments that issuers could account for as equity. Under SFAS No. 150, those instruments with characteristics of both liabilities and equity must be classified as liabilities in the consolidated balance sheets, with the corresponding payments to holders of the instruments recognized as interest expense.

The reporting requirements of SFAS No. 150 are effective July 1, 2003. On October 29, 2003, the FASB agreed to defer provisions related to mandatory redeemable financial instruments to periods beginning after December 15, 2004. The adoption of SFAS No. 150 did not have a material impact on the results of operations or the financial position of the Company.

NOTE 2 ACQUISITIONS

In February 2002, the Bank acquired Asahi Bank of California, a wholly-owned subsidiary of Asahi Bank Ltd Japan, for approximately \$14.9 million. The acquisition was structured as a statutory merger of Asahi Bank of California into the Bank. On the date of acquisition, Asahi Bank of California had total assets of approximately \$50.0 million, including \$35.0 million of commercial real estate and business loans and \$15.0 million of cash and securities which were acquired by the Bank at the closing of the transaction. The Bank recorded \$2.3 million of goodwill in connection with this acquisition. The purpose of this acquisition was to expand the Bank s customer base and to obtain certain commercial banking systems and technology.

On October 25, 2002, the Company acquired the operating assets and the performing film finance loan portfolio of the Lewis Horwitz Organization (LHO) in an all cash transaction valued at approximately \$93.0 million. The Bank recorded \$0.8 million of goodwill in connection with this acquisition. LHO is a lender to the independent film and television production industry. LHO operates as a division of the Bank. The purpose of this acquisition was to diversify the Bank s lending products and expand its customer base.

These acquisitions were accounted for in accordance with SFAS No. 141. The results of operations related to these entities are included in the consolidated statements of income from the date of each respective acquisition.

Table of Contents**NOTE 3 INVESTMENT SECURITIES**

The amortized cost and fair value of investment securities as of December 31, 2003 and 2002 are as follows:

	Amortized Cost	Fair Value	Gross Unrealized	
			Gains	Losses
(in thousands)				
December 31, 2003:				
Investment securities available for sale:				
U.S. Government Agency	\$47,749	\$47,621	\$	\$ 128
Residual interest in securitized loans	5,055	5,368	313	
Equity securities	25	104	88	9
Total investment securities available for sale	\$52,829	\$53,093	\$401	\$ 137
December 31, 2002:				
Investment securities available for sale:				
U.S. Government Agency	\$48,698	\$48,986	\$353	\$ 65
Residual interest in securitized loans	5,305	5,619	314	
Equity securities	25	72	62	15
Total investment securities available for sale	\$54,028	\$54,677	\$729	\$ 80

At December 31, 2003, the carrying value of U.S. government agency securities available for sale consisted of \$21.0 million of securities that mature within three years with an average yield of 2.61%, and \$26.7 million of securities that mature after three but within five years with an average yield of 3.15%. The \$21.0 million of securities that mature within three years are callable as follows: \$3.5 million in April 2004, \$3.5 million in May 2004, \$3.5 million in August 2004, \$7.0 million in November 2004, and \$3.5 million in December 2004. The \$26.7 million of securities that mature after three but within five years are callable as follows: \$7.6 million are callable in January 2004, \$2.1 million are callable in March 2004, \$6.1 million are callable in July 2004, \$8.2 million are callable in August 2004, and \$2.7 million are callable in April 2005.

At December 31, 2002, the carrying value of U.S. government agency securities available for sale consisted of \$14.1 million of securities that mature within three years with an average yield of 4.20%, and \$34.6 million of securities that mature after three but within five years with an average yield of 4.62%. The \$14.1 million of securities that mature within three years are callable as follows: \$3.0 million in February 2003, \$2.0 million in March 2003, \$2.0 million in May 2003, and \$7.1 million in June 2003. The \$34.6 million of securities that mature after three but within five years are callable as follows: \$3.9 million are callable in February 2003, \$6.1 million are callable in April 2003, \$3.0 million are callable in May 2003, \$2.1 million are callable in June 2003, \$9.1 million are callable in August 2003, \$3.0 million are callable in October 2003, and \$7.4 million are callable in November 2003.

During 2003 and 2002, no securities were sold prior to their maturity or call date.

There were no gross realized gains or losses on investment securities for the years ended December 31, 2003, 2002 and 2001.

NOTE 4 LOANS

Loans held in the Bank's portfolio consist of the following:

December 31,	
2003	2002

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

	(in thousands)	
Real estate loans	\$ 1,128,851	\$ 1,069,434
Construction loans	129,540	101,422
Film finance loans	98,630	119,283
Franchise loans	102,128	54,672
Commercial and other loans	6,869	4,314
	<u>1,466,018</u>	<u>1,349,125</u>
Unamortized premium	2,904	3,858
Deferred loan origination fees, net of costs	(500)	(5,604)
	<u>1,468,422</u>	<u>1,347,379</u>
Allowance for loan losses	(31,573)	(31,081)
	<u>\$ 1,436,849</u>	<u>\$ 1,316,298</u>

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Table of Contents

At December 31, 2003, approximately 89.9%, 9.9% and 0.2% of the Bank's loans collateralized by real estate were secured by income producing properties, properties under development and residential one-to-four family properties, respectively. At December 31, 2003, approximately 72.7% of our loans secured by real estate were collateralized by properties located in California.

At December 31, 2002, approximately 92.1%, 7.7% and 0.2% of the Bank's loans collateralized by real estate were secured by income producing properties, properties under development and residential one-to-four family properties, respectively. At December 31, 2002, approximately 73.1% of our loans secured by real estate were collateralized by properties located in California.

At December 31, 2003 and 2002, approximately \$791.8 million and \$606.9 million, respectively, of loans were pledged to secure a borrowing facility at the Federal Home Loan Bank (FHLB) of San Francisco.

The following is the activity in the allowance for loan losses on loans for the periods indicated.

	As of and for the Years Ended December 31,		
	2003	2002	2001
	(in thousands)		
Balance at beginning of year	\$31,081	\$24,722	\$22,608
Provision for loan losses	7,860	9,030	7,225
Additions related to acquisitions		2,048	
Charge-offs:			
Real estate loans	(5,286)	(4,730)	(2,845)
Construction loans			(2,419)
Commercial/Industrial loans	(1,461)		
Consumer loans	(700)		
Total charge-offs	(7,447)	(4,730)	(5,264)
Recoveries:			
Real estate loans	14	11	153
Consumer loans	65		
Total recoveries	79	11	153
Net charge-offs	(7,368)	(4,719)	(5,111)
Balance at end of year	\$31,573	\$31,081	\$24,722

As of December 31, 2003 and 2002, the accrual of income had been suspended on approximately \$7.7 million and \$5.9 million, respectively, of bank loans. Interest income that was contractually due on loans that were on nonaccrual status that was not recognized during the years ended December 31, 2003, 2002 and 2001 was approximately \$608,000, \$941,000, and \$2.1 million, respectively.

As of December 31, 2003 and 2002, restructured loans totaled \$8.4 million and \$7.9 million, respectively. There were no related commitments to lend additional funds on restructured loans. For the years ended December 31, 2003, 2002 and 2001, \$775,000, \$905,000, and \$376,000, respectively, of gross interest income would have been recorded had the loans been current in accordance with their original terms compared to \$696,000, \$796,000, and \$340,000, respectively, of interest income that was included in net income for the same periods. The average yield on restructured loans was 6.93% and 8.05%, respectively at December 31, 2003 and 2002.

The Bank's recorded investment in impaired loans, and the related valuation allowance, were as follows:

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

	December 31, 2003		December 31, 2002	
	Recorded Investment	Valuation Allowance	Recorded Investment	Valuation Allowance
	(in thousands)			
Valuation allowance required	\$ 6,255	\$ 1,242	\$ 7,251	\$ 1,622
No valuation allowance required	6,830		8,702	
Total impaired loans	\$ 13,085	\$ 1,242	\$ 15,953	\$ 1,622

\$3.5 million of the impaired loans with a valuation allowance were on nonaccrual status at December 31, 2003. The average recorded investment in impaired loans for the years ended December 31, 2003, 2002 and 2001 was \$13.1 million, \$11.6 million, and \$26.0 million, respectively. Interest income recognized on impaired loans for the years ended December 31, 2003, 2002 and 2001 was \$475,000, \$375,000, and \$89,000, respectively.

Loans having carrying values of \$9.6 million and \$3.5 million were transferred to OREO in 2003 and 2002, respectively.

Table of Contents**NOTE 5 ICCMAC MULTIFAMILY AND COMMERCIAL TRUST 1999-1**

Real estate loans held in trust consisted of the following:

	December 31,	
	2003	2002
	(in thousands)	
Real estate loans	\$ 67,878	\$ 119,824
Unamortized premium	2,525	4,040
	70,403	123,864
Allowance for loan losses	(1,828)	(1,928)
	\$ 68,575	\$ 121,936

The following is the activity in the allowance for loan losses relating to real estate loans held in the ICCMAC Trust as follows:

	December 31,	
	2003	2002
	(in thousands)	
Balance at beginning of year	\$ 1,928	\$ 1,928
Reversal of provision for loan losses	(100)	
Charge-offs		
Balance at end of year	\$ 1,828	\$ 1,928

At December 31, 2003 and 2002, the recorded investment in impaired loans of the ICCMAC Trust was \$810,000 and \$233,000, respectively. There was no valuation allowance required on these loans. The average recorded investment in impaired real estate loans of the ICCMAC Trust was \$321,000 and \$345,000 at December 31, 2003 and 2002, respectively. There was no interest income recognized on the ICCMAC Trust impaired loans for the years ended December 31, 2003, 2002 and 2001.

The following is a summary of the outstanding CMOs of the ICCMAC Trust:

Class	Recorded Amount December 31,		Interest Rate Margin over 6 month LIBOR	Rating
	2003	2002		
	(in thousands)			
A-2	\$	\$24,015	0.42%	AAA
S	190	1,511	zero coupon	AAA
A-3		17,447	0.60%	AAA
B	1,146	11,631	0.88%	AA
C	14,539	14,539	1.55%	A

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

	15,875	69,143
Unamortized Discount	(7)	(66)
	\$ 15,868	\$ 69,077

The interest rate on the variable rate CMOs adjusts monthly and the repayment of the bonds is based on the cash flows of the underlying loan portfolio.

NOTE 6 OTHER REAL ESTATE OWNED

Other real estate owned was stated as follows:

	December 31,	
	2003	2002
	(in thousands)	
Other real estate owned held for sale	\$ 7,548	\$ 13,086
Less: valuation allowance	(500)	(493)
Other real estate owned, net	\$ 7,048	\$ 12,593

Table of Contents

The activity in the valuation allowance for other real estate owned was as follows:

	As of and for the Years Ended December 31,		
	2003	2002	2001
	(in thousands)		
Balance at beginning of year	\$ 493	\$ 374	\$ 127
Provision for losses on other real estate owned	870	796	269
Charge-offs upon sale of other real estate owned	(863)	(677)	(22)
	<u>500</u>	<u>493</u>	<u>374</u>
Balance at end of year	\$ 500	\$ 493	\$ 374

NOTE 7 PREMISES AND EQUIPMENT

Premises and equipment are stated at cost less accumulated depreciation and amortization and consist of the following:

	December 31,	
	2003	2002
	(in thousands)	
Furniture, fixtures and equipment	\$ 9,542	\$ 7,383
Leasehold improvements	5,351	5,039
Automobiles	842	522
	<u>15,735</u>	<u>12,944</u>
Accumulated depreciation and amortization	(9,969)	(8,747)
	<u>\$ 5,766</u>	<u>\$ 4,197</u>

Depreciation and amortization expense on premises and equipment for the years ended December 31, 2003, 2002 and 2001 was \$1.7 million, \$946,000, and \$836,000, respectively.

NOTE 8 DEPOSIT ACCOUNTS

Deposit accounts consist of the following:

	December 31,	
	2003	2002
	(in thousands)	
Non-interest demand accounts	\$ 9,074	\$
Interest demand accounts	38,518	
Money market and passbook accounts	156,505	168,525
Time certificates under \$100,000	564,207	521,404
Time certificates \$100,000 and over	378,713	375,982

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

\$ 1,147,017

\$ 1,065,911

Demand deposit accounts have no contractual maturity. Interest bearing demand accounts pay interest at rates ranging from 1.29% to 1.90% per annum. The weighted average contractual interest rate of the Bank's interest-bearing demand deposit accounts was 1.86% at December 31, 2003. Money market and passbook accounts have no contractual maturity and pay interest at rates ranging from 0.25% to 3.54% per annum. The weighted average contractual interest rate of the Bank's money market and passbook accounts was 1.63% and 1.67% at December 31, 2003 and 2002, respectively. Additionally, some money market accounts have limited checking features which allow three check withdrawals per month. Time certificates have maturities ranging from 30 days to five years and bear interest at varying rates based on market conditions, ranging from 0.95% to 6.53% per annum. The weighted average contractual interest rate of the Bank's time certificate accounts was 2.24% and 2.90% at December 31, 2003 and 2002, respectively.

Interest expense on time certificates \$100,000 and over for the years ended December 31, 2003, 2002 and 2001 amounted to approximately \$8.7 million, \$9.0 million, and \$16.1 million, respectively.

The Bank is a member of the FDIC and its deposits are insured up to \$100,000 each per insured depositor.

Table of Contents

As of December 31, 2003, the contractual maturities of time certificate accounts were as follows:

Year of Maturity	Amount
	(in thousands)
2004	\$726,191
2005	146,761
2006	43,367
2007	6,382
2008	20,219
	<u>\$942,920</u>

NOTE 9 LINES OF CREDIT

As of December 31, 2003 and 2002, the Bank had uncommitted, unsecured lines of credit with two banks renewable daily in the amount of \$30.0 million. There were no borrowings against these lines at December 31, 2003 and 2002.

NOTE 10 JUNIOR SUBORDINATED DEBENTURES

The Company has created five trusts, Trust I, Trust II, Trust III, Trust IV, and Trust V. Trust I issued \$14.0 million of 10.60% cumulative trust preferred securities in September 2000, Trust II issued \$15.0 million of 10.20% cumulative trust preferred securities in February 2001, Trust III issued \$20.0 million of variable rate cumulative trust preferred securities, Trust IV issued \$10.0 million of variable rate cumulative trust preferred securities, and Trust V issued \$25.0 million of variable rate cumulative trust preferred securities, (referred to collectively as the Trust Preferred securities). ITLA Capital has fully and unconditionally guaranteed the Trust Preferred securities along with all obligations of each trust under their respective trust agreements. Each trust was formed for the exclusive purpose of issuing their respective Trust Preferred securities and common securities and using the proceeds to acquire ITLA Capital's junior subordinated deferrable interest debentures. Trust I acquired an aggregate principal amount of \$14.4 million of ITLA Capital's 10.60% junior subordinated deferrable interest debentures due September 7, 2030 that pays interest each March 7 and September 7 during the term of this security. Trust II acquired an aggregate principal amount of \$15.5 million of ITLA Capital's 10.20% junior subordinated deferrable interest debentures due February 22, 2031 that pays interest each February 22 and August 22 during the term of this security. Trust III acquired an aggregate principal amount of \$20.6 million of ITLA Capital's variable rate junior subordinated deferrable interest debentures due October 30, 2032 that pays interest on each April 30 and October 30 during the term of the security. Trust IV acquired an aggregate principal amount of \$10.3 million of ITLA Capital's variable rate junior subordinated deferrable interest debentures due December 10, 2032 that pays interest each June 15 and December 15 during the term of the security. Trust V acquired an aggregate principal amount of \$25.8 million of ITLA Capital's variable rate junior subordinated deferrable interest debentures due December 26, 2032 that pays interest quarterly on March 26, June 26, September 26, and December 26 during the term of the security. The sole assets of each trust are the debentures it holds. Each of the debentures is redeemable, in whole or in part, at ITLA Capital's option on or after ten years after issuance for Trust I and Trust II (at declining premiums for the first ten years and at par thereafter until maturity), and five years after issuance for Trust III, Trust IV, and Trust V (at par until maturity). Each of the debentures is also redeemable, in whole and not in part, at ITLA Capital's option any time prior to maturity, upon the occurrence of certain special events, which include, among others, a determination by the Federal Reserve Board that the Trust Preferred securities do not qualify as Tier 1 capital (discussed below).

The Company used the proceeds from the debentures for general corporate purposes, including an aggregate of \$81.3 million in capital contributions to the Bank to support future growth. The costs associated with the Trust Preferred securities issuance were netted with proceeds and are being amortized using a method that approximates the interest method over a period of five to ten years. The distributions paid on the Trust Preferred securities are reflected as Minority interest in income of subsidiary in the Consolidated Statements of Income. Minority interest in income of subsidiary was \$6.1 million, \$3.5 million, and \$3.0 million for the years ended December 31, 2003, 2002 and 2001, respectively.

Prior to the adoption of FIN 46, the Trust Preferred securities were reflected on the Consolidated Balance Sheets as Guaranteed Preferred Beneficial Interests in the Company's Junior Subordinated Deferrable Interest Debentures. The recorded balance of Trust Preferred securities was \$81.6 million at December 31, 2002. At December 31, 2003, upon adoption of FIN 46, the Company was required to deconsolidate the Trusts from its financial statements. As a result of the deconsolidation, the debentures are included in Junior subordinated debentures and the Company's investment interests in the Trusts and deferred debt issuance costs are included in Other assets on the Consolidated Balance Sheets.

Table of Contents

The trust preferred securities however, qualify as Tier 1 capital for ITLA Capital under Federal Reserve Board guidelines. As a result of the issuance of FIN 46, the Federal Reserve Board is currently evaluating whether deconsolidation of the trusts will affect the qualification of the trust preferred securities as Tier 1 capital. As of December 31, 2003, the Company would meet all requirements to maintain the well capitalized designation regardless of the inclusion of the capital securities in Tier 1 capital.

NOTE 11 FHLB ADVANCES

FHLB advances represent collateralized obligations with the FHLB of San Francisco, and are summarized by contractual maturity as follows:

Year of Maturity	Amount
	(in thousands)
2004	\$ 307,600
2005	1,100
2006	32,905
2007	
2008	11,000
Thereafter	9,530
	<u>\$ 362,135</u>

We have pledged real estate loans with a carrying value of \$791.8 million, and cash equivalents and investment securities available for sale with a carrying value of \$47.6 million, for a total of \$839.4 million of assets pledged as collateral for this borrowing facility. The total borrowing capacity available from the collateral that has been pledged is approximately \$531.6 million, of which \$169.5 million remained as of December 31, 2003.

The following table represents the maximum month-end balance outstanding, weighted-average daily balance outstanding, average rates paid during the year, and the average rates on the balance at year-end for FHLB advances:

	December 31,		
	2003	2002	2001
	(dollars in thousands)		
Maximum month-end balance outstanding	\$ 362,135	\$ 338,685	\$ 269,285
Weighted-average daily balance outstanding	\$ 201,419	\$ 194,160	\$ 103,675
Average rates paid during the year	2.57%	2.92%	4.62%
Average rates on balance at year-end	1.69%	1.99%	2.99%
Balance at year-end	\$ 362,135	\$ 338,685	\$ 269,285

NOTE 12 RESIDUAL INTEREST IN SECURITIZATION

During the first quarter of 2002, the Company formed a qualified special purpose entity (QSPE) to issue \$86.3 million of asset-backed notes in a securitization of substantially all of the Company's residential loan portfolio. The Company recognized a gain of \$3.7 million on the securitization of these loans, which was included in other non-interest income within the consolidated statement of income. Concurrent with recognizing such gain on sale, the Company recorded a residual interest of \$5.6 million, which represented the present value of future cash flows (spread and fees) that are estimated to be received over the life of the loans. The residual interest is recorded on the consolidated balance sheet in

Investment securities available for sale, at fair value. The value of the residual interest is subject to substantial credit, prepayment, and interest rate risk on the sold residential loans. In accordance with the provisions of SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities, the residual interest is classified as available for sale and, as such, recorded at fair value with the resulting changes in fair value recorded as accumulated unrealized gain or loss in a separate component of shareholders' equity entitled Accumulated other comprehensive income or loss, until realized. Fair value is estimated on a monthly basis using a discounted cash flow analysis. These cash flows are estimated over the lives of the receivables using prepayment, default, and interest rate assumptions that management believes market participants would use for similar financial instruments.

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

During 2003, the Company recognized an other than temporary impairment of \$1.0 million on the residual interest. Impairments that are deemed to be other than temporary are charged to non-interest income. In evaluating impairments as other than temporary the Company considers credit risk, as well as the magnitude and trend of default rates and prepayment speeds of the underlying residential loans.

Table of Contents

At December 31, 2003 and 2002, key economic assumptions and the sensitivity of the current fair value of the residual interest based on projected cash flows to immediate adverse changes in those assumptions are as follows:

	December 31, 2003	December 31, 2002
Dollars in thousands		
Fair value of retained interest	\$ 5,368	\$ 5,619
Weighted average life (in years) securities	0.90	1.49
Weighted average life (in years) residual interest	4.47	4.70
Weighted average annual prepayment speed	35.0%	35.0%
Impact of 10% adverse change	\$ (67)	\$ (23)
Impact of 25% adverse change	\$ (120)	\$ (59)
Weighted average annual discount rate	15.0%	15.0%
Impact of 10% adverse change	\$ (147)	\$ (167)
Impact of 25% adverse change	\$ (367)	\$ (404)
Weighted average lifetime credit losses	3.3%	3.3%
Impact of 10% adverse change	\$ (313)	\$ (285)
Impact of 25% adverse change	\$ (753)	\$ (678)

These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in the fair value of the residual interest are based on a variation in assumptions and generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, in the above table, the effect of a variation in a particular assumption on the fair value of the residual interest is calculated without changing any other assumption; in reality, changes in one factor may result in changes in another (for example, increases in market interest rates may result in lower prepayments but increased credit losses), which might magnify or counteract the sensitivities, and depending on the severity of such changes, the results of operations may be materially affected.

NOTE 13 BENEFIT PLANS

Salary Savings Plan. The Company has a salary savings plan (the Savings Plan) that qualifies as a deferred salary arrangement under Section 401(k) of the Internal Revenue Code. Under the Savings Plan, participating employees may defer a portion of their pretax earnings, not to exceed the annual limits established by the Internal Revenue Service. We match 50% of each employee's salary deferral, up to a maximum 6% of the employee's salary. Employees vest in employer contributions and the earnings thereon over a five-year period. Matching contributions to the Savings Plan were \$357,000, \$189,000, and \$112,000 in 2003, 2002 and 2001, respectively.

Nonqualified Deferred Compensation Plans. The Company has deferred compensation plans designed to provide additional retirement benefits for certain officers and key employees who cannot take full advantage of the Savings Plan. There were no costs associated with these deferred compensation plans in 2003, 2002 and 2001.

Long-Term Supplemental Executive Retirement Plan. The Company has adopted a Long-Term Supplemental Executive Retirement Plan (the SERP) for certain officers and key employees which provides for participants to be awarded shares of common stock of the Company on a tax deferred basis from the current Recognition and Retention Plan (RRP) previously approved by the shareholders. Such shares vest in three-year cycles or earlier at the discretion of the Compensation Committee of the Board of Directors, and once vested, may be distributed to participants upon a change in control or the participant's death, disability, retirement date or date of termination of employment. During 1998, the Company issued shares of common stock, representing the remaining number of unissued shares authorized to be awarded under the RRP, to a Rabbi Trust managed by a third-party financial institution. For 2003, 2002 and 2001, 21,158, 20,880 and 30,685 shares, respectively, were allocated to designated SERP accounts for the future benefit of certain Company executives. The Company recognized \$189,000, \$476,000, and \$674,000 of compensation expense from the SERP/RRP in 2003, 2002 and 2001, respectively.

Stock Plans. The Company adopted an employee stock incentive plan and stock option plan for nonemployee directors (collectively, the Stock Plan) which provides for the award of up to 1,311,500 shares of common stock to officers, directors and employees as compensation for future services, not to exceed a combined 550,000 shares during 1995, the first year of the Stock Plan, with annual awards thereafter limited to 100,000 additional shares. An amendment to the Stock Plan increasing the number of shares authorized for award under the Stock Plan by 311,500 shares was approved by the Company's shareholders on June 29, 2001. As of December 31, 2003, the Company has granted an aggregate of 1,554,750 options under the Stock Plan, of which 327,294 have been exercised and 374,673 have been forfeited. The exercise price per share of the options granted ranges from \$10.00 to \$46.69 per share and generally vest 33-1/3% per year, beginning with the first anniversary of the date of each individual grant.

Table of Contents

The number of options and weighted-average exercise prices of options for each of the following groups of options, for the periods indicated, are as follows:

	Number of Options		Weighted-Average Exercise Prices	
	2003	2002	2003	2002
Options outstanding at the beginning of the year	1,067,000	814,250	\$ 16.86	\$ 13.07
Options granted during the year	24,000	298,750	\$ 38.37	\$ 27.39
Options exercised during the year	(220,880)	(13,665)	\$ 13.12	\$ 13.49
Options forfeited during the year	(17,337)	(32,335)	\$ 24.92	\$ 18.31
Options outstanding at the end of the year	852,783	1,067,000	\$ 18.35	\$ 16.86
Options exercisable at the end of the year	638,238	713,917	\$ 15.17	\$ 12.86

The fair value of each option grant was estimated on the date of grant using an option pricing model with the following weighted-average assumptions for option grants:

	Weighted-Average Assumptions for Options Grants		
	2003	2002	2001
Dividend Yield	0.00%	0.00%	0.00%
Expected Volatility	38.04%	31.36%	30.41%
Risk-Free Interest Rates	3.65%-4.34%	4.62%-4.88%	4.79% - 5.13%
Expected Lives	Seven Years	Seven Years	Seven Years
Weighted-Average Fair Value	\$ 14.75-\$21.84	\$ 10.12-\$13.46	\$ 7.14-\$8.37

NOTE 14 INCOME TAXES

Deferred income taxes reflect the net effect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes.

Significant components of our deferred tax assets and liabilities are as follows:

	December 31,	
	2003	2002
	(in thousands)	
Components of the deferred tax asset:		
Allowance for loan losses	\$ 13,339	\$ 13,307
Accrued expenses	2,103	3,217
State income taxes	1,262	1,266
Other real estate owned	460	745
Other	278	
Total deferred tax assets	17,442	18,535

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Components of the deferred tax liability:		
Deferred loan origination costs	3,723	2,326
FHLB stock dividends	1,999	1,886
Unrealized gain on investment securities available for sale	111	297
Other		204
Total deferred tax liabilities	5,833	4,713
Net deferred tax asset	\$11,609	\$13,822

The deferred tax asset is considered fully realizable, as when the temporary differences associated with the deferred tax asset are recognized for income tax purposes, those deductions are expected to be fully offset, either by carryback against previously taxed income or by reducing future taxable income. Accordingly, we have not established a valuation allowance on the deferred tax asset.

Table of Contents

A summary of the provision for income taxes follows:

	Years Ended December 31,		
	2003	2002	2001
	(in thousands)		
Current provision:			
Federal	\$ 13,131	\$ 11,127	\$ 9,824
State	3,416	3,916	2,115
	<u>16,547</u>	<u>15,043</u>	<u>11,939</u>
Deferred provision (benefit):			
Federal	1,835	(462)	(1,007)
State	564	(1,793)	461
	<u>2,399</u>	<u>(2,255)</u>	<u>(546)</u>
	<u>\$ 18,946</u>	<u>\$ 12,788</u>	<u>\$ 11,393</u>

A reconciliation of the federal statutory income tax rate to the effective income tax rate is as follows:

	Years Ended December 31,		
	2003	2002	2001
Federal statutory income tax rate	35.0%	35.0%	35.0%
State income tax, net of federal income tax benefit	7.0%	7.0%	7.0%
State income tax credit and other benefits	(3.0)%	(3.0)%	(3.4)%
	<u>39.0%</u>	<u>39.0%</u>	<u>38.6%</u>

The income tax benefit (expense) component of other comprehensive income was \$186,000, \$(302,000), and \$21,000 for the years ended December 31, 2003, 2002 and 2001, respectively.

NOTE 15 FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK

We are a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of our customers. These financial instruments consist of commitments to extend credit. These instruments may involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheet. The contractual amounts of those instruments reflect the extent of involvement we have in particular classes of financial instruments.

We have exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit. This exposure is represented by the contractual amount of those instruments and the Company uses the same lending policies for these instruments as it does for the loan portfolio. We had outstanding unfunded loan commitments, including the unfunded portion of construction loans, of approximately \$153.5 million and \$91.2 million at December 31, 2003 and 2002, respectively.

Unfunded commitments under commercial lines of credit, revolving credit lines and overdraft protection agreements are commitments for possible extensions of future extensions of credit to existing customers. These lines of credit are typically uncollateralized and usually do not contain a specific maturity date and may not be drawn upon to the total extent to which the Company is committed. We had outstanding

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

commercial lines of credit totaling \$66.1 million at December 31, 2003. There were no outstanding commercial lines of credit at December 31, 2002.

Table of Contents**NOTE 16 COMMITMENTS AND CONTINGENCIES****Commitments**

We lease office facilities under noncancelable operating leases. Estimated future minimum lease payments required under leases with initial or remaining noncancelable terms in excess of one year at December 31, 2003 are as follows:

	(in thousands)
2004	\$ 2,632
2005	2,657
2006	2,624
2007	2,590
2008	698
Thereafter	181
	<hr/>
Sub-Lease income	(1,531)
	<hr/>
	\$ 9,851
	<hr/>

Certain leases contain rental escalation clauses based on increases in the consumer price index, and renewal options of up to ten years, which may be exercised by the Company. We incurred rent expense of \$2.9 million, \$2.1 million, and \$2.1 million in 2003, 2002 and 2001, respectively.

Contingencies

We are subject to various pending legal actions which arise in the normal course of business. We maintain reserves for losses from legal actions which are both probable and estimable. Although the amount of the ultimate exposure, if any, cannot be determined at this time, in management's opinion, based upon advice of counsel, the disposition of claims currently pending will not have a material adverse effect on our financial condition or results of operations.

NOTE 17 REGULATORY REQUIREMENTS

The Company, the Bank's holding company, is subject to supervision by the Federal Reserve Board (FRB). The Bank is subject to supervision and regulation by the FDIC and the Department of Financial Institutions (DFI) of the State of California under the provisions of the California Banking Law. These provisions authorize the Bank's issuance of deposits, place limits on the size of loans the Bank can make, and specify the maintenance of minimum liquidity levels.

The Company and the Bank are also subject to various capital requirements administered by the FRB and FDIC, respectively. The FRB and the FDIC have substantially similar risk-based capital ratio and leverage ratio guidelines for banking organizations. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary action by regulators that, if undertaken, could have a direct material effect on the Company's consolidated financial statements and the Bank's operations. Under the applicable capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of the Company's and the Bank's assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The Company's and the Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios (set forth in the following table) of Total and Tier 1 capital to risk-weighted assets, and of Tier 1 capital to average total assets (Leverage Ratio). Management believes, as of December 31, 2003 and 2002, that the Company and the Bank meet all applicable capital adequacy requirements.

As of December 31, 2003, the most recent notification from the FDIC categorized the Bank as well capitalized under the applicable regulatory framework. Similarly, the Company's capital levels exceeded the levels necessary to be considered well capitalized. To be categorized as well capitalized, the Company and the Bank must maintain minimum Total Risk-Based, Tier 1 Risk-Based and Tier 1 Leverage Ratios as set

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

forth in the following table. There are no conditions or events since that notification that management believes have changed the Company's and the Bank's category. The Company commenced operations as a bank holding company in January 2003, and therefore, was not subject to the regulatory capital guidelines in 2002.

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Table of Contents

The capital securities held by the subsidiary trusts qualify as Tier 1 capital for the Company under Federal Reserve Board guidelines. As a result of the issuance of FIN 46, the FRB is currently evaluating whether deconsolidation of the trusts will affect the qualification of the capital securities as Tier 1 capital. If in the future it is determined that the capital securities can no longer qualify as Tier 1 capital, the Company would still meet all capital adequacy requirements to which it is subject.

ITLA Capital and the Bank's actual regulatory capital amounts and ratios are presented in the following table:

	Actual		Minimum Requirement for Capital Adequacy Purposes		Capital Required to Maintain "Well Capitalized" Designation	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(dollars in thousands)						
As of December 31, 2003						
Total capital (to risk-weighted assets)						
ITLA Capital	\$ 284,952	18.2%	\$ 125,444	8.0%	\$ 156,805	10.0%
Imperial Capital Bank	\$ 233,746	15.6%	\$ 120,170	8.0%	\$ 150,213	10.0%
Tier I capital (to risk-weighted assets)						
ITLA Capital	\$ 244,745	15.6%	\$ 62,722	4.0%	\$ 94,083	6.0%
Imperial Capital Bank	\$ 214,813	14.3%	\$ 60,085	4.0%	\$ 90,128	6.0%
Tier I capital (to average total assets)						
ITLA Capital	\$ 244,745	14.2%	\$ 69,081	4.0%	\$ 86,351	5.0%
Imperial Capital Bank	\$ 214,813	13.2%	\$ 64,964	4.0%	\$ 81,205	5.0%
As of December 31, 2002						
Total capital (to risk-weighted assets)						
Imperial Capital Bank	\$ 202,623	14.4%	\$ 112,238	8.0%	\$ 140,298	10.0%
Tier I capital (to risk-weighted assets)						
Imperial Capital Bank	\$ 184,910	13.2%	\$ 56,119	4.0%	\$ 84,179	6.0%
Tier I capital (to average total assets)						
Imperial Capital Bank	\$ 184,910	13.1%	\$ 63,848	4.0%	\$ 71,013	5.0%

Additionally, Federal and state banking regulations place certain restrictions on dividends paid and loans or advances made by the Bank to the Company. The total amount of dividends which may be paid at any date is generally limited to the retained earnings of the Bank, and loans or advances are limited to 10 percent of the Bank's capital stock and surplus on a secured basis.

At December 31, 2003, the Bank's retained earnings available for the payment of dividends was \$83.8 million. Accordingly, \$134.1 million of the Company's equity in the net assets of the Bank was restricted at December 31, 2003. Funds available for loans or advances by the Bank to the Company amounted to \$13.4 million. In addition, dividends paid by the Bank to the Company would be prohibited if the effect thereof would cause the Bank's capital to be reduced below applicable minimum capital requirements.

Table of Contents**NOTE 18 EARNINGS PER SHARE**

The following is a reconciliation of the amounts used in the calculation of Basic earnings per share and Diluted earnings per share.

	<u>Net Income</u>	<u>Weighted-Average Shares Outstanding</u>	<u>Per Share Amount</u>
(in thousands, except per share data)			
Year ended December 31, 2003			
Basic earnings per share	\$29,634	6,030	\$ 4.91
Dilutive effect of stock options		480	(0.36)
	<u>\$29,634</u>	<u>6,510</u>	<u>\$ 4.55</u>
Diluted earnings per share	\$29,634	6,510	\$ 4.55
Year ended December 31, 2002			
Basic earnings per share	\$20,005	5,979	\$ 3.35
Dilutive effect of stock options		360	(0.19)
	<u>\$20,005</u>	<u>6,339</u>	<u>\$ 3.16</u>
Diluted earnings per share	\$20,005	6,339	\$ 3.16
Year ended December 31, 2001			
Basic earnings per share	\$18,151	6,427	\$ 2.82
Dilutive effect of stock options		241	(0.10)
	<u>\$18,151</u>	<u>6,668</u>	<u>\$ 2.72</u>
Diluted earnings per share	\$18,151	6,668	\$ 2.72

NOTE 19 DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value estimates are based on judgments regarding credit risk, expectations of future economic conditions, normal cost of administration of these instruments and other risk characteristics, including interest rate risk and prepayment risk. These estimates are subjective in nature, involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates. The fair value estimates presented do not include the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments.

We use the following methods and assumptions to estimate the fair value of each class of financial instruments for which it is practicable to estimate value:

Cash and Cash Equivalents The carrying values reported in the balance sheet approximate fair values due to the short-term nature of the assets.

Investment Securities Fair values are based on bid prices and quotations published and/or received from established securities dealers.

Stock in Federal Home Loan Bank The carrying value approximates fair value based on the redemption provisions of the FHLB.

Loans and Real Estate Loans Held in Trust The fair value is estimated using the present value of future cash flows, discounted using the current rate at which similar loans would be made to borrowers with similar credit ratings and for the same maturities and giving consideration to estimated prepayment risk and credit risk.

Accrued Interest Receivable The carrying values reported in the balance sheet approximate the fair values due to the short-term nature of the asset.

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Deposit Accounts The fair value of demand deposit, money market and passbook accounts is estimated to be the amount payable on demand due to the short-term nature of these deposits. The fair values for time certificates, both over and under \$100,000, are estimated by discounting the expected cash flows at current market rates over expected maturities.

Federal Home Loan Bank Advances The fair value is estimated by discounting the expected cash flows at current market rates over contractual maturities.

Junior Subordinated Debentures The fair value is estimated using the present value of future cash flows, discounted using the current rate at which a similar debenture would be issued.

Table of Contents

The carrying amounts and estimated fair values of our financial instruments are as follows:

	December 31,			
	2003		2002	
	Cost or Carrying Amount	Estimated Fair Value	Cost or Carrying Amount	Estimated Fair Value
(in thousands)				
Financial assets:				
Cash and cash equivalents	\$ 178,318	\$ 178,318	\$ 160,848	\$ 160,848
Investment securities	53,093	53,093	54,677	54,677
Stock in Federal Home Loan Bank	17,966	17,966	16,934	16,934
Loans, net	1,436,849	1,447,107	1,316,298	1,334,574
Real estate loans held in trust, net	68,575	69,067	121,936	126,127
Accrued interest receivable	8,958	8,958	9,158	9,158
Financial liabilities:				
Deposit accounts	\$ 1,147,017	\$ 1,144,019	\$ 1,065,911	\$ 1,064,491
Federal Home Loan Bank advances	362,135	361,783	338,685	338,729
Collateralized mortgage obligations	15,868	15,872	69,077	69,139
Junior subordinated debentures	86,600	88,000		
Guaranteed preferred beneficial interests in the Company's junior subordinated deferrable interest debentures			81,595	84,670

NOTE 20 BUSINESS SEGMENT INFORMATION

SFAS No. 131, "Disclosures About Segments of an Enterprise and Related Information" requires disclosure of segment information in a manner consistent with the "management approach". The management approach is based on the way the chief operating decision-maker organizes segments within a company for making operating decisions and assessing performance.

The main factors used to identify operating segments were the specific product and business lines of the various operating segments of the Company. Operating segments are organized separately by product and service offered. We have identified one operating segment that meets the criteria of being a reportable segment in accordance with the provisions of SFAS No. 131. This reportable segment is the Company's lending operations, which by its legal form, is identified as operations of the Bank and Imperial Capital REIT. This segment derives the majority of its revenue by originating and purchasing loans. Other operating segments of the Company that did not meet the criteria of being a reportable segment in accordance with SFAS No. 131 have been aggregated and reported as "All Other". Transactions from all of our operating segments occur primarily in the United States. The Company has no transactions with a single external customer that exceeds ten percent of the Company's consolidated revenues.

Transactions between the reportable segment of the Company and its other operating segments are made at terms which approximate arm's-length transactions and in accordance with GAAP. There is no significant difference between the measurement of the reportable segment's assets and profits and losses disclosed below and the measurement of assets and profits and losses in our consolidated balance sheets and statements of income. Accounting allocations are made in the same manner for all operating segments.

Table of Contents

Required reported segment information for 2003, 2002 and 2001 is detailed below:

	<u>Lending Operations</u>	<u>All Other</u>	<u>Eliminations</u>	<u>Consolidated</u>
As of or for the Year Ended December 31, 2003				
Revenues from external customers	\$ 130,851	\$ 1,162	\$ (796)	\$ 131,217
Total interest income	115,452	7,404	(6,879)	115,977
Total interest expense	31,546	6,200	(6,879)	30,867
Depreciation and amortization expense	1,343	379		1,722
Provision for income taxes	20,627	(1,681)		18,946
Capital expenditures	2,787	504		3,291
Deferred income taxes	9,607	1,981	21	11,609
Total assets	1,741,092	350,013	(272,890)	1,818,215
Income (loss) before provision for income taxes	56,472	(7,892)		48,580
As of or for the Year Ended December 31, 2002				
Revenues from external customers	\$ 105,522	\$ 9,835	\$ (4,376)	\$ 110,981
Total interest income	104,652	10,332	(4,376)	110,608
Total interest expense	35,694	6,004	(4,376)	37,322
Depreciation and amortization expense	479	467		946
Provision for income taxes	11,542	1,246		12,788
Capital expenditures	2,612	354		2,966
Deferred income taxes	10,480	3,242	100	13,822
Total assets	1,543,502	511,759	(333,296)	1,721,965
Income (loss) before provision for income taxes	36,069	(3,276)		32,793
As of or for the Year Ended December 31, 2001				
Revenues from external customers	\$ 125,154	\$ 3,329	\$ (4,329)	\$ 124,154
Total interest income	124,109	3,315	(4,329)	123,095
Total interest expense	65,303	2,889	(4,329)	63,863
Depreciation and amortization expense	411	425		836
Provision for income taxes	9,172	2,221		11,393
Capital expenditures	321	431		752
Deferred income taxes	10,840	929	100	11,869
Total assets	1,519,440	200,639	(211,771)	1,508,308
Income (loss) before provision for income taxes	33,064	(3,520)		29,544

NOTE 21 PARENT COMPANY ONLY CONDENSED FINANCIAL STATEMENTS

The parent company only financial statements of ITLA Capital are as follows:

Condensed Balance Sheets

	<u>December 31,</u>	
	<u>2003</u>	<u>2002</u>
	(in thousands)	
Assets		
Cash and cash equivalents	\$ 1,613	\$ 2,338
Investment securities available for sale, at fair value	5,472	5,691
Investments in wholly-owned subsidiaries:		
Imperial Capital Bank	217,891	188,328
Imperial Capital Real Estate Investment Trust	36,099	36,887
Other subsidiaries	253	2,879
Investments in unconsolidated subsidiaries	2,600	
Other assets	16,606	10,951

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Total assets	\$280,534	\$247,074
Liabilities and Shareholders Equity		
Junior subordinated debentures	\$ 86,600	\$ 86,600
Other liabilities	7,035	3,783
Shareholders equity	186,899	156,691
Total liabilities and shareholders equity	\$280,534	\$247,074

Table of Contents**Condensed Statements of Income**

	Years Ended December 31,		
	2003	2002	2001
	(in thousands)		
Interest income	\$ 1,321	\$ 1,059	\$ 302
Interest expense	6,200	3,356	2,889
Net interest expense	(4,879)	(2,297)	(2,587)
Provision (reversal of provision) for loan losses	150	5	(1,200)
Non-interest expense:			
Loss on sale of real estate owned	21		
General and administrative expense	2,589	2,367	2,062
Other	159	707	
Total non-interest expense	2,769	3,074	2,062
Loss before income tax (benefit) expense and equity in net income of subsidiaries	(7,798)	(5,376)	(3,449)
Income tax (benefit) expense	(1,642)	420	2,260
Loss before equity in net income of subsidiaries	(6,156)	(5,796)	(5,709)
Equity in net income of subsidiaries	35,790	25,801	23,860
NET INCOME	\$29,634	\$20,005	\$ 18,151

Condensed Statements of Cash Flows

	Years Ended December 31,		
	2003	2002	2001
	(in thousands)		
Cash Flows From Operating Activities:			
Net income	\$ 29,634	\$ 20,005	\$ 18,151
Adjustments to net income:			
Equity in undistributed net income of subsidiaries	(35,790)	(25,807)	(23,856)
Provision for loan losses	150	5	(1,200)
Other, net	506		
(Increase) decrease in other assets	(5,494)	(4,887)	1,043
Increase in liabilities	3,252	5,423	656
Net cash used in operating activities	(7,742)	(5,261)	(5,206)
Cash Flows From Investing Activities:			
Proceeds from securitization and sale of real estate loans		98,155	
Purchase of loans from Imperial Capital Bank		(98,602)	
Purchases of investment securities available for sale		(5,305)	
Capital contribution to Imperial Capital Bank		(53,348)	(14,549)
Cash paid for common equity of Trust Preferred Securities		(1,691)	(475)
Dividends received from Imperial Capital Bank	2,500	9,000	15,600
	4,236	7,070	5,050

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

Dividends received from Imperial Capital Real Estate Investment Trust			
Other, net	(383)	(143)	539
Net cash provided by (used in) investing activities	6,353	(44,864)	6,165
Cash Flows From Financing Activities:			
Proceeds from issuance of trust preferred securities		53,389	14,549
Proceeds from exercise of employee stock options	2,897	184	74
Cash paid to acquire treasury stock	(2,233)	(2,343)	(14,759)
Net cash provided by (used in) financing activities	664	51,230	(136)
Net (decrease) increase in cash and cash equivalents	(725)	1,105	823
Cash and cash equivalents at beginning of period	2,338	1,233	410
Cash and cash equivalents at end of period	\$ 1,613	\$ 2,338	\$ 1,233

Table of Contents

NOTE 22 SUBSEQUENT EVENT

In January 2004, the Company entered into an agreement with an unaffiliated bank for two revolving lines of credit of \$25.0 million each. The lines of credit mature on March 31, 2004 and January 1, 2005, respectively. Interest accrues at a variable rate based on the one month LIBOR rate and the lines are secured by the outstanding capital stock of the Bank. The primary purpose of the lines is to provide additional capital funding in connection with the strategic business relationship with Household relating to certain tax refund products.

Table of Contents

Item 9. Changes In and Disagreements With Accountants on Accounting and Financial Disclosure

On May 29, 2002, the Board of Directors of the Company dismissed the Company's independent auditors, Arthur Andersen LLP, and upon recommendation by its Audit Committee, approved the engagement of Ernst & Young LLP as the Company's independent auditors for the year ending December 31, 2002.

The reports of Arthur Andersen LLP on the Company's financial statements as of and for the years ended December 31, 2001 and 2000, did not contain an adverse opinion or a disclaimer of opinion and were not qualified or modified as to uncertainty, audit scope, or accounting principles.

During the Company's fiscal years ended December 31, 2001 and 2000, and the subsequent interim period from January 1, 2002 through May 29, 2002, there were no disagreements with Arthur Andersen LLP on any matters of accounting principles or practices, financial statement disclosure, or auditing scope and procedures which, if not resolved to the satisfaction of Arthur Andersen LLP would have caused Arthur Andersen LLP to make reference to the matter in their report. There were no reportable events as that term is defined in Item 304(a)(1)(v) of Regulation S-K.

Prior to the dismissal of Arthur Andersen LLP, the Company did not consult with Ernst & Young LLP regarding: (i) the application of accounting principles to a specified transaction, either completed or proposed; (ii) the type of audit opinion that might be rendered on the Company's financial statement; or (iii) a reportable event (as defined in paragraph 304(a)(1)(v) of Regulation S-K).

The Company requested Arthur Andersen LLP to furnish it with a letter addressed to the Commission stating whether it agreed with the above statements. A copy of that letter, dated June 4, 2002, is filed as Exhibit 16 to the Current Report on Form 8-K filed by the Company on June 5, 2002.

Item 9A. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures: An evaluation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the "Act")) was carried out as of December 31, 2003 under the supervision and with the participation of the Company's Chief Executive Officer, Chief Financial Officer and several other members of the Company's senior management. The Company's Chief Executive Officer and Chief Financial Officer concluded that as of December 31, 2003, the Company's disclosure controls and procedures were effective in ensuring that the information required to be disclosed by the Company in the reports it files or submits under the Act is (i) accumulated and communicated to the Company's management (including the Chief Executive Officer and Chief Financial Officer) in a timely manner, and (ii) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

(b) Changes in Internal Controls: During the quarter ended December 31, 2003, no change occurred in the Company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Table of Contents**PART III****Item 10. Directors and Executive Officers of the Registrant****Executive Officers and Directors of the Registrant**

The executive officers of the Registrant are identified below.

<u>Name</u>	<u>Age</u>	<u>Position</u>
George W. Haligowski	49	Chairman of the Board, President and Chief Executive Officer of ITLA Capital and the Bank
Norval L. Bruce	62	Vice Chairman of the Board and Chief Credit Officer of ITLA Capital and the Bank
Timothy M. Doyle	47	Senior Managing Director and Chief Financial Officer of ITLA Capital and the Bank
Don Nickbarg	51	Senior Managing Director and Chief Banking Officer of ITLA Capital and the Bank
William A. Schack	42	Managing Director Deputy Chief Credit Officer-Administration of ITLA Capital and the Bank
William K. Callam	47	Managing Director Deputy Chief Credit Officer-Production of ITLA Capital and the Bank
Scott A. Wallace	41	Managing Director Chief Administrative Officer of ITLA Capital and the Bank
Anthony A. Rusnak	40	Deputy Managing Director General Counsel of ITLA Capital and the Bank

George W. Haligowski has served as ITLA Capital's Chairman of the Board, President and Chief Executive Officer since inception. He has also served as the Bank's Chairman of the Board and Chief Executive Officer since 1992, and was the Bank's President from 1992 to October 1997. In 2000 he was again appointed as President of the Bank. From 1990 to the present, he has also served as President, Chief Executive Officer and Principal of Halivest International, Ltd., an international finance and asset management company. He was previously employed as a Vice President by Shearson Lehman Hutton (1988 to 1990) and Prudential-Bache Securities (1983 to 1988), and by Avco Financial Services as Regional Director of its Japanese branch operations (1976 to 1981), as Training Coordinator for Avco Thrift and Loan (1976) and as a Branch Manager (1974 to 1976).

Norval L. Bruce has served as the Vice Chairman and Chief Credit Officer for ITLA Capital and the Bank since June of 1999. He was previously President and Chief Operating Officer of the Bank from October 1997 to June 1999, and previously was the Executive Vice President and Chief Credit Officer of the Bank from 1990 to October 1997. Mr. Bruce was appointed a director of the Bank and the Company in January 1997 and September 1997, respectively. From 1988 to 1989, he served as Executive Vice President and Chief Credit Officer of Security Pacific Bank, Nevada. He was previously employed by Security Pacific Bank from 1965 to 1988 in a variety of positions including management positions in which he was responsible for both loan origination and credit quality.

Timothy M. Doyle has served as Senior Managing Director and Chief Financial Officer of ITLA Capital and the Bank since May 2000. He was previously Managing Director and Chief Administrative Officer of ITLA Capital and the Bank since 1996. Before joining the Bank, he was the Controller and Director of Operations at Northeastern Plastics from 1995 to 1996; Assistant Controller of Alpha Wire Corporation from 1992 to 1994; and Vice President and Chief Financial Officer of Halivest International, Ltd. from 1989 to 1991. From 1982 to 1988, he was the Corporate Controller of the Shepaug Corporation.

Don Nickbarg has served as Senior Managing Director and Chief Banking Officer of ITLA Capital and the Bank since November 2002. He has served in several other capacities, including Senior Managing Director and Chief Operating Officer, Managing Director of Asset Acquisition and New Business Development, Chief Administrative Officer as well as Treasurer. Prior to joining ITLA Capital in 1998, he was a consultant with Centennial International LLC from 1996 to 1998; Chief Financial Officer of AIOC Corporation from 1994 to 1996; Vice President and Team Leader at The Chase Manhattan Bank from 1991 to 1994; Vice President and Treasurer of Drexel Burnham Lambert Holdings, Ltd. from 1986 to 1990; Vice President with The Hong Kong and Shanghai Banking Company from 1980 to 1986; and Assistant Treasurer with the Swiss Bank Corporation from 1976 to 1980.

Edgar Filing: ITLA CAPITAL CORP - Form 10-K

William A. Schack has served as Managing Director Deputy Chief Credit Officer-Administration of ITLA Capital and the Bank since November 2002. Prior to that he was Managing Director Director of Operations of the Bank from August 2001 to November 2002 and First Vice President Director of Portfolio Management and Loan Administration of the Bank from April 2001 to August 2001. Prior to joining ITLA Capital he was Senior Vice President Chief Operating Officer of First Bank of Beverly Hills from 1999

Table of Contents

through 2001 and served in various senior management capacities with First Bank since 1997. He has also held senior managerial positions with First Los Angeles Bank and Western Federal Savings Bank from 1990 through 1995.

Scott A. Wallace has served as Managing Director Chief Administrative Officer of ITLA Capital and the Bank since November 2001. He was previously Deputy Managing Director and Chief Accounting Officer of ITLA Capital and the Bank from October 1999 until October 2001 and was Vice President Controller of the Bank from September 1996 until October 1999. Prior to joining the Bank in September 1996, he was Vice President Finance of Westfield Corporation, Inc. in 1996 and was Vice President Controller of First Los Angeles Bank in 1995. From 1984 to 1994, he was a senior manager with Kenneth Leventhal & Company.

William K. Callam has served as Managing Director Deputy Chief Credit Officer Production of ITLA Capital and the Bank since November 2002. He was previously First Vice President and Director of Loan Operations, and Vice President and Chief Appraiser, since joining the Bank in December 1999. Prior to joining the Bank, he was Vice President Team Leader with Bank of America, and its predecessor, Security Pacific National Bank, from 1989 to 1999, with an interim position as Vice-President and Chief Appraiser of First Los Angeles Bank in 1994 to 1995.

Anthony A. Rusnak has served as ITLA Capital and the Bank s Deputy Managing Director General Counsel and Corporate Secretary since November 1997. Prior to joining us, he was in private practice for seven years representing financial institutions, businesses, corporations and individuals in business, real estate transactions and litigation. Previously, he worked for law firms in the San Diego area, as well as for San Diego Gas and Electric s corporate in-house counsel.

The directors of the Company, excluding Mr. Haligowski and Mr. Bruce, are identified below.

Preston Martin, age 80, is the former Vice Chairman of the Federal Reserve Board of Governors. Mr. Martin previously served as a Senior Advisory Director to the Board. Mr. Martin is currently Chairman of the Board of Martin Associates, a San Francisco based financial services company. Mr. Martin was Chairman and Chief Executive Officer of Seraro Corporation, a Sears Roebuck enterprise, PMI Mortgage Insurance Corporation and PMI Mortgage Corporation. Mr. Martin was also Professor of Finance and Director of Executive Programs at the University of Southern California.

Jeffrey L. Lipscomb, age 50, is an Investment Advisory Associate with AXA Advisors and formerly was a Registered Principal and Assistant Manager of the San Diego office of Equitable Financial Companies since 1986, handling corporate group benefits and personal financial planning, and also was with Kidder Peabody from 1983 to 1986.

Sandor X. Mayuga, age 56, is a member of the California State Bar and has been a member of the law firm of Tisdale & Nicholson since 1994. He conducted his own law practice from 1983 to 1994 and was a partner in the Financial Institutions Department of Finley, Kumble, Wagner, Heine, Underberg, Manly & Casey, a New York-based national law firm, from 1980 to 1983. Previously, he served as Assistant General Counsel of Hunt-Wesson Foods, Inc., a subsidiary of Norton Simon, Inc., and was associated with two large regional law firms in Los Angeles County. Since 1980, Mr. Mayuga s practice has focused on the representation of financial institutions and other finance-related businesses in corporate, transactional and regulatory matters.

Hirota Oribe, age 69, is a licensed architect with international experience in real estate development and urban planning. Since 1993, Mr. Oribe has served as an advisor to Kajima Development Resources, Inc. From 1979 to 1993, Mr. Oribe was Executive Vice President, Chief Operating Officer and a Director of Kajima Development Corporation, a firm engaged in development and construction of single-family and multi-family housing, office buildings, retail space and land development. Mr. Oribe previously held other positions with affiliates of Kajima Corporation of Japan from 1973 to 1979 and was a practicing architect from 1962 to 1973.

Robert R. Reed, age 67, is retired from Household International where he was employed in various positions from 1960 to 1992. Mr. Reed served as Vice President of Household Bank from 1980 to 1992. Mr. Reed was previously employed in management positions with Household Financial Corporation from 1962 to 1980. From 1995 to 2000, Mr. Reed served as a director of the Santa Ana City Cable Television Review Board.

Audit Committee Membership

The Audit Committee of ITLA Capital s Board of Directors consists of Directors Martin (Chairman), Lipscomb and Reed. The Board of Directors has determined that Mr. Martin is an audit committee financial expert, as defined in the SEC s rules, and that Mr. Martin is independent, as independence is defined for audit committee members in the listing standards of the NASDAQ Stock Market.

Table of Contents**Code of Ethics**

We have adopted a code of ethics that applies to our principal executive officer, principal financial officer, principal accounting officer, and persons performing similar functions, and to all of our other employees and our directors. A copy of our code of ethics is available on our website, located at www.itlacapital.com.

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934 requires ITLA Capital's directors and executive officers, and persons who own more than 10% of a registered class of our equity securities, to file with the SEC initial reports of ownership and reports of changes in ownership of common stock and other equity securities of ITLA Capital. Officers, directors and greater than 10% stockholders are required by SEC regulation to furnish ITLA Capital with copies of all Section 16(a) forms they file.

To our knowledge, based solely on a review of the copies of such reports furnished to us and written representations that no other reports were required, during the fiscal year ended December 31, 2003, all Section 16(a) filing requirements applicable to its officers, directors and greater than 10% beneficial owners were complied with, except for the inadvertent failure to timely file a Form 3 by Joseph Ursino, a former officer of ITLA Capital.

Item 11. Executive Compensation

The following table sets forth the compensation of the Chief Executive Officer and the four other highest earning executive officers of ITLA Capital and the Bank with salary and bonus greater than \$100,000 for the year ended December 31, 2003 (the "named executives").

Name and Principal Position	Year	Annual Compensation		Long-Term Compensation	All Other Compensation (\$)
		Salary (\$)	Bonus (\$)	Options (#) (1)	
George W. Haligowski Chairman of the Board, President and Chief Executive Officer	2003	\$496,202	\$998,775(2)		\$231,081(3)
	2002	\$443,350	\$579,000(2)	37,500	\$309,583
	2001	\$397,515	\$457,125(2)		\$780,761
Norval L. Bruce Vice Chairman of the Board, and Chief Credit Officer	2003	\$230,769(8)	\$159,504(8)		\$47,642(4)
	2002	\$217,469(8)	\$115,265(8)	20,000	\$83,654
	2001	\$200,538(8)	\$96,502(8)		\$132,872
Timothy M. Doyle Senior Managing Director and Chief Financial Officer	2003	\$193,917	\$141,004		\$32,607(5)
	2002	\$180,726	\$98,314	15,000	\$63,707
	2001	\$166,633	\$80,186		\$107,919
Don Nickbarg Senior Managing Director and Chief Banking Officer	2003	\$175,528	\$103,003(9)		\$26,767(6)
	2002	\$163,004	\$64,990(9)	15,000	\$69,555
	2001	\$130,946	\$62,550(9)	10,000	\$23,547
Scott Wallace Managing Director and Chief Administrative Officer	2003	\$149,084	\$69,503		\$23,457(7)
	2002	\$139,545	\$63,005	5,000	\$24,613
	2001	\$124,515	\$40,000	3,000	\$8,387

(1) Options were granted on various dates and vest one-third on each of the three subsequent anniversary dates of issuance.

(2) \$400,000 of the 2003 bonus was deferred at the election of the named executive officer under ITLA

Capital s
Nonqualified
Deferred
Compensation
plan. The
respective
amounts were
\$400,000 and
\$200,000 in
2002 and
2001.(3) Consists
of (a) \$23,000
in auto related
benefits, (b)
\$30,000 in
supplemental
housing
payments, (c)
\$56,845 in life
insurance
premiums, (d)
\$6,000 in
employer
contributions
to ITLA
Capital s
401(k) plan,
(e) \$32,940 in
preferential
interest on
employee
savings
accounts in
2003, and
(f) an
allocation of
9,144 shares of
restricted stock
under the
Supplemental
Executive
Retirement
Plan ("SERP")
valued at \$9.00
per share (see
"Supplemental
Executive
Retirement
Plan" below)
for an
aggregate
value of
\$82,296.(4) Consists
of (a) \$2,379 in
auto related
benefits, (b)
\$3,233 in life
insurance
premiums, (c)
\$6,000 in
employer
contributions

*to ITLA
Capital s
401(k) plan,
(d) \$13,026 in
preferential
interest on
employee
savings
accounts in
2003, and
(e) an
allocation of
2,556 shares of
restricted stock
under the
Supplemental
Executive
Retirement
Plan ("SERP")
valued at \$9.00
per share (see
"Supplemental
Executive
Retirement
Plan" below)
for an
aggregate
value of
\$23,004.*

Table of Contents

- (5) Consists of (a) \$1,851 in auto related benefits, (b) \$6,000 in employer contributions to ITLA Capital s 401(k) plan, (c) \$5,253 in life insurance benefits in 2003, and (d) an allocation of 2,167 shares of restricted stock under the Supplemental Executive Retirement Plan ("SERP") valued at \$9.00 per share (see "Supplemental Executive Retirement Plan" below) for an aggregate value of \$19,503.
- (6) Consists of
(a) \$1,818 in auto related benefits,
(b) \$6,000 in employer contributions to ITLA Capital s 401(k) plan,
(c) \$824 in life insurance benefits in 2003, (d) \$629 in preferential interest on employee savings accounts in 2003, and
(e) an allocation of 1,944 shares of restricted stock under the Supplemental Executive Retirement Plan ("SERP") valued at \$9.00 per share (see "Supplemental Executive Retirement Plan" below) for an aggregate value of \$17,496.(7) Consists of (a) \$1,583 in auto related benefits,
(b) \$6,000 in employer contributions to ITLA Capital s 401(k) plan,
(c) \$298 in life insurance benefits in 2003, (d) \$573 in preferential interest on employee

savings
accounts in
2003, and
(e) an
allocation of
1,667 shares of
restricted stock
under the
Supplemental
Executive
Retirement
Plan ("SERP")
valued at
\$9.00 per
share (see
"Supplemental
Executive
Retirement
Plan" below)
for an
aggregate
value of
\$15,003.(8) \$115,385
of the 2003
salary and
none of the
2003 bonus
was deferred at
the election of
the named
executive
officer under
ITLA
Capital s
Nonqualified
Deferred
Compensation
plan. The
respective
amounts were
\$108,735 and
\$57,633 in
2002 and
\$100,269 and
\$48,251 in
2001.(9) \$20,000
of the 2003
bonus was
deferred at the
election of the
named
executive
officer under
ITLA
Capital s
Nonqualified
Deferred
Compensation
plan. The
respective
amounts were
\$10,000 in

2002 and none
in 2001.

Option Grants for 2003

No stock options or stock appreciation rights have been granted to the named executive officers in 2003 pursuant to the Stock Option Plan.

Option Exercises and Values at December 31, 2003

The following table sets forth certain information concerning the number and value of stock options at December 31, 2003 held by the named executive officers.

Option Values at December 31, 2003

Name	Shares Acquired on Exercise (#)	Value Realized (\$)	Number of Unexercised Option at Fiscal Year-End (#)		Value of Unexercised "In-the-Money" Options at Fiscal Year-End (1)(\$)	
			Exercisable	Unexercisable	Exercisable	Unexercisable
George W. Haligowski	100,000	\$ 3,992,800	272,500	25,000	\$ 10,274,750	\$ 667,500
Norval L. Bruce	60,968	2,200,514	40,698	13,334	1,435,659	361,351
Timothy M. Doyle		n/a	65,000	10,000	2,243,325	271,000
Don Nickbarg		n/a	26,666	13,334	919,911	383,989
Scott Wallace		n/a	20,666	4,334	700,217	97,403

(1) The difference between the aggregate option exercise price and the closing price of \$50.10 of the underlying shares at December 31, 2003.

Agreements with Mr. Haligowski

We have entered into an employment agreement with Mr. Haligowski. The employment agreement provides for an initial employment term of five years, with the agreement automatically annually extending for an additional one-year period each year unless either party provides the other with at least 90 days notice of the non-extension or termination. The employment agreement provides that we may terminate Mr. Haligowski for cause, as defined in the employment agreement. In the event Mr. Haligowski is involuntarily terminated, as defined in the employment agreement, including following a change of control, as defined in the employment agreement, Mr. Haligowski will be entitled to receive during the remaining term of the agreement his base salary calculated at the highest annual rate during the three years prior to his involuntary termination and the average amount of cash bonus and incentive compensation paid for the two years prior to his involuntary termination, if any, the continuation of all employment

Table of Contents

related benefits for the 60 months following the date of termination and the immediate vesting of any stock options and restricted stock awards previously granted and outstanding. As a result of a change of control, Mr. Haligowski will also be retained as a consultant for an eighteen month period following the change in control at a monthly consulting fee equal to 75% of his base salary and an additional contribution to his account in our Supplemental Executive Retirement Plan equal to 3.95 times his base salary. In addition, the terms of the employment agreement shall be extended 60 months and stock options and restricted stock awards previously granted and outstanding, salary continuation plans, equity club memberships and other fringe benefits shall immediately vest following a change of control. The annual base salary for Mr. Haligowski under the employment agreement is currently \$447,500 (which may be increased from time to time by the Board of Directors). The employment agreement also provides for, among other things, annual incentive compensation, disability pay, participation in stock benefit and salary continuation plans, and other fringe benefits, including a supplemental housing payment of not less than \$2,500 per month, an automobile allowance of not less than \$1,950 per month, and life insurance coverage in an amount not less than four times Mr. Haligowski's annual salary. In addition we shall maintain health, dental and life insurance benefits for the 60 months following an involuntary termination and transfer title to our owned vehicle currently used by Mr. Haligowski. In March 2000, we adopted a Salary Continuation Plan for the benefit of Mr. Haligowski. Under the terms of this plan, Mr. Haligowski will be entitled to receive monthly payments, based on 75% of his average monthly base salary for the three years preceding the year in which the plan benefits become payable, for a 15 year period. The benefits under the plan become payable on the earlier of Mr. Haligowski's retirement upon reaching age 65, or his death, disability, or involuntary termination (other than a termination for cause, as defined in the agreement). If Mr. Haligowski voluntarily terminates his employment prior to reaching age 65, the benefit payable to him under the plan will be prorated based on the ratio of the actual period that he worked while the plan is in effect to the scheduled period of time that he would have worked if he had continued to work until reaching age 65. If we undergo a change of control, the vesting of plan benefits accelerates and become payable monthly over a ten-year period, with an increased monthly payment to reflect the shorter payment period.

Change of Control Agreements

We have entered into change of control agreements with Messrs. Bruce, Doyle, Nickbarg and Wallace. The change in control agreements have initial terms of one year and shall automatically extend for additional one-year periods upon a change of control, as defined in the agreement, or upon their anniversary date, unless either party provides the other with at least 90 days notice of termination. These agreements provide that in the event the officer is involuntarily terminated within 24 months following a change of control, as defined in the agreement, the officer shall be entitled to receive upon such termination an amount equal to the greater of the annualized salary as in effect on the date of the change of control or the date of termination for a period of up to 18 months and a pro rata portion of his bonus from the previous year. In addition we will maintain health, dental and life insurance benefits for up to the next 18 months for each officer and transfer title to our owned vehicle currently used by the officer or, in the event the officer receives a monthly cash car allowance in lieu of the use of our vehicle, we shall pay an amount equal to up to 18 times the monthly allowance. Stock options and restricted stock awards previously granted and outstanding will also immediately vest. The annual base salary for Messrs. Bruce, Doyle, Nickbarg and Wallace is currently \$230,000, \$195,000, \$175,000 and \$150,000, respectively.

Both Mr. Haligowski's employment agreement and the change of control agreements also provide that to the extent any payments made may be considered excess parachute payments under Section 280G of the Internal Revenue Code that are subject to excise tax, we will pay an additional amount needed to insure that the amount of payments and value of benefits received equals the same amount in the absence of any excise tax.

Supplemental Executive Retirement Plan (SERP)

The SERP provides that the compensation committee may make restricted stock awards under ITLA Capital's Recognition and Retention Plan (RRP) on a tax deferred basis through the SERP. The SERP further provides that Mr. Haligowski shall receive an allocation annually, subject to the performance terms of the RRP, of a restricted stock award equal to one-third of his base salary and all other participants shall receive an award equal to one-fifth of base salary subject to the approval of the compensation committee, which may also allocate a greater or lesser award or no award in its discretion. For this purpose, each share of common stock has been valued at \$9.00 per share, the fair market value of the common stock on the date of issuance to the SERP. A participant shall only have a vested right to amounts allocated to his or her account if the participant is employed on the last day of a three year vesting cycle or earlier at the discretion of the compensation committee. Upon a change in control (as defined in the SERP), the participant shall have an accelerated vesting of all shares allocated to his or her account. The participant shall only have a right to vested shares in his or her account upon normal retirement, death, disability or termination. The last day of the next vesting cycle for shares allocated to the SERP accounts for the benefit of the participants for the years 2003, 2004 and 2005 is December 31, 2005. For additional discussion, please see *Benefits Recognition and Retention Plan*.

Table of Contents

Benefits

Insurance Plans. All full-time employees, after approximately three months employment with us, are covered under group plans providing major medical, dental, and vision benefits, and long-term disability, travel accident, accidental death and dismemberment insurance, and group term life insurance.

Salary Savings Plan. The ITLA Capital Salary Savings Plan is a cash or deferred arrangement under Section 401(k) of the Internal Revenue Code (the Code) designed to provide employees with the opportunity to accumulate retirement funds (the 401(k) Plan). Permanent employees age 21 or older are eligible to participate in the 401(k) Plan as of January 1 or July 1 first following their hire date. Under the 401(k) Plan, subject to limitations imposed under Section 401(k) and Section 415 of the Code, a participant may elect to defer compensation by directing us to contribute such amount to the 401(k) Plan on such employee's behalf. We currently make matching contributions to the 401(k) Plan equal to 50% of the first 6% of the participant's monthly contribution. The Board reviews the match on an annual basis, and we may also make discretionary contributions to the 401(k) Plan. Compensation for purposes of the 401(k) Plan is defined as a participant's compensation from us as reported annually on Form W-2, including contributions to the 401(k) Plan by the employee, and contributions by us in the employee's behalf to any other pension, insurance, welfare or other employee benefit plan. Under the 401(k) Plan, a separate account is established for each participant. Participants are always 100% vested in their contributions and the earnings thereon. Participants become vested in employer contributions and the earnings thereon at the rate of 20% per year commencing with the first full year of service (defined as completion of 12 consecutive months of work). Participants become fully vested in employer contributions and the earnings thereon on their fifth anniversary of employment, or in the event of death, permanent disability or attainment of age 65 while employed by us. The 401(k) Plan provides for in-service hardship distributions of elective deferrals, as well as loans of a portion of vested account balances. Distributions from the 401(k) Plan are made upon termination of service in a lump sum or in annual installments over a period of years at the election of the participant with the right to take a lump sum payment at any time during such period.

Nonqualified Deferred Compensation Plans. The ITLA Capital Corporation Supplemental Salary Savings Plan (the Supplemental Plan) and Nonqualified Deferred Compensation Plan (the Deferral Plan) are designed to provide additional retirement benefits for certain officers and highly compensated employees. The Supplemental Plan provides participating employees with an opportunity to make up benefits not available under the 401(k) Plan due to any application of limitations on compensation and maximum benefits under the 401(k) Plan. Benefits under the Supplemental Plan are provided at the same time and in the same form as benefits under the 401(k) Plan, and become taxable to the participant at that point. The Deferral Plan allows a participant to defer receipt of, and current taxation upon, designated portions of the participant's direct cash compensation until a future date specified by the participant. Both of these plans are unfunded plans, meaning that all benefits payable there under are payable from our general assets, and funds available to pay benefits are subject to the claims of our general creditors. We have established a Rabbi Trust with a third party FDIC insured financial institution which holds the contributions to the Supplemental Plan and Deferral Plan, for the purpose of providing the benefits set forth under the terms of the plans. Participants only have the rights of unsecured creditors with respect to the Rabbi Trust assets.

Stock Plans. We have adopted the 1995 Employee Stock Incentive Plan and the 1995 Stock Option Plan for Nonemployee Directors (collectively, the Stock Option Plan) pursuant to which officers, directors and our employees are eligible to receive options to purchase Common Stock. The purpose of the Stock Option Plan is to enable us to attract, retain and motivate employees by providing for or increasing their proprietary interests in ITLA Capital, and in the case of nonemployee directors, to attract such directors and further align their interests with our interests. Every one of our employees is eligible to be considered for the grant of awards under the Stock Option Plan. An amendment to the Stock Plan increasing the number of shares authorized for awards under the Stock Plan by 311,500 shares was approved by the Company's shareholders on June 29, 2001. The maximum number of shares of Common Stock that may be issued pursuant to awards granted under the Stock Option Plan is 1,311,500 shares of which a maximum of 550,000 shares may be awarded during the first year of the Stock Option Plan, with annual awards thereafter limited to 100,000 additional shares during each of the next five years of the Stock Option Plan (with the shares subject to the Stock Option Plan and all grants there under being subject to adjustments to prevent dilution).

The Stock Option Plan is administered by the Compensation Committee of the Board of Directors, except that grants to nonemployee directors are made by the Board of Directors pursuant to a predetermined formula, as described below. The Committee consists of two or more nonemployee directors of ITLA Capital, and has full and final authority to select the employees to receive awards and to grant such awards. Subject to provisions of the Stock Option Plan, the Committee has a wide degree of flexibility in determining the terms and conditions of awards and the number of shares to be issued pursuant thereto. The expenses of administering the Stock Option Plan are borne by us.

Table of Contents

The Stock Option Plan authorizes the Committee to enter into any type of arrangement with an eligible employee that, by its terms, involves or might involve the issuance of Common Stock or any other security or benefit with a value derived from the value of Common Stock. Awards to employees are not restricted to any specified form or structure. Stock options to purchase 5,000 shares of Common Stock were automatically granted to the nonemployee directors upon the completion of our initial public offering and upon their election to the Board of Directors, and options to purchase an additional 1,000 shares are granted annually for the following five years, provided such individuals continue to serve as directors.

Awards may not be granted under the Stock Option Plan after the tenth anniversary of the adoption of the Stock Option Plan. We have granted an aggregate of 1,554,750 options under the Stock Option Plan, of which 397,500 have been granted to Mr. Haligowski, 115,000, 75,000, 40,000 and 25,000 have been granted to Messrs. Bruce, Doyle, Nickbarg, and Wallace, respectively, 46,000 have been granted to non-employee directors, and 856,250 have been granted to other employees, of which 327,294 have been exercised and 374,673 have been forfeited. The exercise price per share of the options granted range from \$10.00 to \$46.69 per share and will generally vest 33-1/3% per year, beginning with the first anniversary of the date of the grant.

Recognition and Retention Plan. We have adopted the Recognition and Retention Plan (RRP), the purpose of which is to promote our long-term interests and our shareholders by providing a means for attracting and retaining officers and employees of ITLA Capital and its affiliates. Under the RRP, awards of restricted shares of our common stock may be made to employees as additional long-term incentive compensation. Every one of our employees is eligible to be considered for the grant of awards under the RRP. The maximum number of shares of common stock which may be issued pursuant to the RRP is 300,000 shares over the ten year life of the plan. No RRP shares may be granted in any fiscal year in which the Bank fails to maintain an adequately capitalized designation under the FDIC regulations and ITLA Capital fails to achieve a return on average assets of at least 50 basis points for the fiscal year. The RRP was approved by the shareholders and is administered by the Compensation Committee of the Board of Directors which has a wide degree of flexibility, within the provisions of the RRP, in determining the terms and conditions of awards and the number of shares to be issued pursuant thereto. The RRP shares granted to date have been allocated through the Supplemental Executive Retirement Plan as discussed above.

Directors Compensation

Directors Fees. During 2003, each non-employee director was paid a monthly fee of \$2,250 for serving on our Board of Directors and \$750 for each Board or Committee meeting attended for service on such committee. In addition, Director Reed received an honorarium of \$5,000 for his active assistance in legislative matters during 2003 and Director Oribe received an honorarium of \$15,000 for his time and assistance with Japanese business matters and his extensive work with the Executive Committee. In 2003, Director Martin received a monthly retainer fee of \$1,250 for his service as Chairman of the Audit Committee.

Voluntary Retainer Stock and Deferred Compensation Plan. In 1996, we adopted the Voluntary Retainer Stock and Deferred Compensation Plan for Outside Directors (the Outside Director Plan). The Outside Director Plan provides for the deferral of compensation earned by non-employee directors in the form of Stock Units (Stock Units) in a Stock Unit account (Stock Unit Account). Directors may elect to have up to 100% of their fees converted into stock units.

For dividends paid with respect to our common stock, each non-employee director has credited to his Stock Unit Account an additional number of Stock Units in an amount determined under the Outside Director Plan. Each non-employee director's Stock Unit Account will be settled by delivering to the non-employee director (or his beneficiary) the number of shares of our common stock equal to the number of whole Stock Units then credited to the non-employee director's Stock Unit Account, in either (i) a lump sum or (ii) substantially equal annual installments over a period not to exceed ten years.

To date, no amounts have been deferred under the Outside Director Plan.

Directors Stock Option Plans. Directors are also eligible to receive stock option grants as described above. On October 30, 2003, Preston Martin was granted an option to purchase 1,000 shares of common stock with an exercise price of \$46.69 per share. The option vests in full on October 30, 2004 and will expire on October 30, 2013. No other options were granted to Directors during 2003.

Compensation Committee Interlocks and Insider Participation

During 2003, the Compensation Committee was comprised of Directors Lipscomb and Oribe.

Table of Contents**Item 12. Security Ownership of Certain Beneficial Owners and Management**

At March 8, 2004, we had 6,268,673 shares of common stock outstanding.

The following table sets forth, as of March 8, 2004, certain information as to those persons who were known by management to be beneficial owners of more than five percent of our common stock outstanding.

Beneficial Owner	Shares Beneficially Owned	Percent of Class
Eubel Brady & Suttman Asset Management Inc. 7777 Washington Village Drive, Suite 210 Dayton, Ohio 45459	511,107(1)	8.15%
Franklin Mutual Advisors, LLC 466,396(2) 7.44%51 John F. Kennedy Parkway Short Hills, NJ 07078 Friedman, Billings, Ramsey Group, Inc. 446,800(3) 7.13%1001 19th Street North Arlington, VA 22209 George W. Haligowski 461,468(4) 7.04%888 Prospect Street, Suite 110 La Jolla, CA 92037 Dimensional Fund Advisors 425,600(5) 6.79%1299 Ocean Avenue, 11th Floor Santa Monica, California 90401 Thomson Horstmann & Bryant, Inc. 375,200(6) 5.98%Park 80 West, Plaza Two Saddle Brook, NJ 07663 Wellington Management Company, LLP 368,400(7) 5.87%75 State Street Boston, MA 02109 Barclays Global Investors, NA 325,497(8) 5.19%45 Fremont Street San Francisco, CA 94105		

(1) *As reported by Eubel Brady & Suttman Asset Management, Inc. (Suttman) on a Schedule 13G amendment filed on February 17, 2004 with the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended. Suttman reported sole voting and dispositive power as to none of the 511,107 shares, and shared voting and dispositive power as to all of the 511,107 shares covered by the report.*

(2) *As reported by Franklin Mutual Advisors, LLC (Franklin) on a Schedule 13G amendment filed on February 9, 2004 with the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended. Franklin reported sole voting and*

dispositive powers as to all of the 466,396 shares, and shared voting and dispositive powers as to none of the 466,396 shares covered by the report.(3) As reported by Friedman, Billings, Ramsey Group, Inc. (FBR) on a Schedule 13G amendment filed on February 17, 2004 with the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended. FBR reported sole voting and dispositive powers as to none of the 446,800 shares, and shared voting and dispositive powers as to all of the 446,800 shares covered by the report.(4) Includes 285,000 shares underlying stock options which are currently exercisable or which will become exercisable within 60 days of March 8, 2004.(5) As reported by Dimensional Fund Advisors (Dimensional) on a Schedule 13G amendment filed on February 6, 2004 and filed with the Securities and Exchange

*Commission
under the
Securities
Exchange Act of
1934, as
amended.
Dimensional
reported sole
voting and
dispositive
powers as to all
of the 425,600
shares, and
shared voting and
dispositive
powers as to none
of the 425,600
shares covered by
the report.*

Table of Contents

(6) *As reported by Thomson Horstmann & Bryant, Inc. (Thomson) on a Schedule 13G amendment filed on January 21, 2004 with the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended. Thomson reported shared voting and dispositive power as to none of the 375,200 shares, sole voting power as to 181,600 shares, and sole dispositive power as to all of the 375,200 shares covered by the report.*

(7) *As reported by Wellington Management Company, LLP (WMC) on a Schedule 13G amendment filed on February 12, 2004 with the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended. WMC reported sole voting and dispositive powers as to none of the 368,400 shares, shared voting power as to 167,800 shares, and shared dispositive power as to all of the 368,400 shares covered by the report.*(8) *As reported by Barclays Global Investors, NA., Barclays Global Fund Advisors, Barclays Global Investors, Ltd., Barclays Global Investors Japan Trust and Banking Company*

Limited,
Barclays Life
Assurance
Company
Limited,
Barclays Bank
PLC.,
Barclays
Capital
Securities
Limited,
Barclays
Capital Inc.,
Barclays
Private Bank
& Trust (Isle
of Man)
Limited,
Barclays
Private Bank
and Trust
(Jersey)
Limited,
Barclays Bank
Trust
Company
Limited,
Barclays Bank
(Suisse) SA.,
and Barclays
Private Bank
Limited, on a
Schedule 13G
filed on
February 17,
2004 with the
Securities and
Exchange
Commission
under the
Securities
Exchange Act
of 1934, as
amended.
With respect
to the 325,497
shares listed,
Barclays
Global
Investors,
NA., reported
sole voting
and
dispositive
powers as to
245,329
shares, and
shared voting
and
dispositive
powers as to
none of such

shares, and Barclays Global Fund Advisors reported sole voting and dispositive powers as to 46,093 shares, and shared voting and dispositive powers as to none of such shares.

The following table sets forth, as of March 8, 2004, certain information as to the shares of common stock beneficially owned by the directors and named executive officers and by all directors and executive officers of ITLA Capital as a group.

Beneficial Owner	Shares Beneficially Owned (1)	Percent of Class
George W. Haligowski	461,468	7.04%
Timothy M. Doyle	96,943	1.53
Norval L. Bruce	92,663	1.47
Don Nickbarg	40,427	0.64
Scott Wallace	24,238	0.39
Sandor X. Mayuga	10,800	0.17
Jeffrey L. Lipscomb	10,400	0.17
Hiroataka Oribe	10,200	0.16
Robert R. Reed	10,200	0.16
Preston Martin	5,666	0.09
All Directors and Executive Officers as a Group (13 Persons)	809,533	11.89

(1) Includes shares held directly, as well as an aggregate of 539,195 shares which are subject to immediately exercisable options and options exercisable within 60 days of March 8, 2004, under ITLA Capital's Stock Option Plan, vested shares held by the SERP, and shares held in retirement accounts or by certain members of the named individual's families or corporations for which an individual is an officer or director or held by trust of which an individual is trustee or a substantial beneficiary, over which shares the individual may be deemed to have sole or shared voting and/or dispositive power. The above named individuals held exercisable options and options exercisable within 60 days of March 8, 2004 as follows: Chairman Haligowski 285,000 shares; Director Lipscomb 10,000 shares; Director Mayuga 10,000 shares; Director Oribe 10,000 shares; Director Reed 10,000 shares; Director Martin 5,000 shares; Norval L. Bruce 47,365 shares; Timothy M. Doyle 70,000 shares; Don Nickbarg 31,666 shares and Scott Wallace 20,667 shares.

Table of Contents

The following table sets forth information as of December 31, 2003 with respect to compensation plans under which shares of our common stock may be issued:

Equity Compensation Plan Information

Plan Category	Number of Shares to be issued upon Exercise of Outstanding Options, Warrants and Rights	Weighted Average Exercise Price of Outstanding Options, Warrants and Rights	Number of Shares Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Shares Reflected in the First Column) (1)
Equity compensation plans approved by stockholders	852,783	\$ 15.17	256,423
Equity compensation plans not approved by stockholders	N/A	N/A	N/A
Total	852,783	\$ 15.17	256,423

(1) This amount includes 125,000 shares issuable under our 1996 Voluntary Retainer Stock and Deferred Compensation Plan for Outside Directors, described under Item 11. Executive Compensation Directors Compensation. Under the Company's 1995 Employee Stock Option and Incentive Plan, up to all of the 126,423 shares remaining available for issuance under that plan as of December 31, 2003 could be issued to plan participants pursuant to awards of restricted stock, performance shares and/or performance units.

Item 13. Certain Relationships and Related Transactions

During the year, we utilized the services of Tisdale & Nicholson. Director Mayuga is a partner in that law firm. During 2003, this law firm received \$155,218 in legal fees from ITLA Capital and the Bank.

Item 14. Principal Accountant Fees and Services

During the fiscal years ended December 31, 2003 and 2002, Ernst & Young LLP provided various audit, audit related and non-audit services to the Company. Set forth below are the aggregate fees billed for these services:

- (a) Audit Fees: Aggregate fees billed for professional services rendered for the audit of the Company's annual financial statements and reviews of financial statements included in the Company's Quarterly Reports on Form 10-Q for those fiscal years: \$225,250 - 2003; \$181,000 - 2002.
- (b) Audit Related Fees: Aggregate fees billed for professional services rendered related to audits of employee benefit plans, and consultation on accounting matters: \$70,000 - 2003; \$17,250 - 2002.
- (c) Tax Fees: Aggregate fees billed for professional services rendered related to tax compliance, tax advice and tax return preparation: \$101,000 - 2003; \$91,600 - 2002.
- (d) All other fees: None - 2003; None - 2002.

The audit committee preapproves all audit and permissible non-audit services to be provided by Ernst & Young LLP and the estimated fees for these services.

Table of Contents**PART IV****Item 15. Exhibits, Financial Statement Schedules and Reports on Form 8-K****(a)(1) Financial Statements:**

Our consolidated financial statements, and Report of Independent Public Accountants thereon, are included in this Form 10-K at the pages listed below:

	Page
Report of Independent Auditors	38
Report of Predecessor Independent Public Accountant	39
Consolidated Balance Sheets as of December 31, 2003 and 2002	40
Consolidated Statements of Income for the Years Ended December 31, 2003, 2002 and 2001	41
Consolidated Statements of Changes in Shareholders' Equity and Comprehensive Income for the Years Ended December 31, 2003, 2002 and 2001	42
Consolidated Statements of Cash Flows for the Years Ended December 31, 2003, 2002 and 2001	43
Notes to Consolidated Financial Statements	44

(a)(2) Financial Statement Schedules:

All financial statement schedules have been omitted as the required information is inapplicable or has been included in the Notes to Consolidated Financial Statements.

Table of Contents**(a)(3) Exhibits:**

Regulation S-K Exhibit Number	Document	Reference to Prior Filing or Exhibit Number Attached Hereto
3.1	Certificate of Incorporation	**
3.2	Bylaws, as amended	*****
4	Instruments Defining the Rights of Security Holders, Including Indentures	None
10.1	1995 Stock Option Plan For Nonemployee Directors	*
10.2	1995 Employee Stock Incentive Plan	*****
10.3a	Nonqualified (Non-Employer Securities) Deferred Compensation Plan	*****
10.3b	Nonqualified (Employer Securities Only) Deferred Compensation Plan	*****
10.4	Supplemental Salary Savings Plan	*
10.5	Data Processing Agreement	*
10.6	Employment Agreement with George W. Haligowski	*
10.7	Change of Control Agreements	***
10.8	Recognition and Retention Plan	**
10.9	Voluntary Retainer Stock and Deferred Compensation Plan for Outside Directors	**
10.10	Supplemental Executive Retirement Plan	*****
10.11	ITLA Capital Corporation Rabbi Trust Agreement	***
10.12	Salary Continuation Plan	****
10.13	Licensing Agreement, dated October 30, 2002, between Imperial Capital Bank and Beneficial Franchise Company, Inc.	*****
10.14	Amended and Restated Sale and Servicing Agreement for RALs and RACs, dated as of January 3, 2003, between Imperial Capital Bank, Household Tax Masters Inc., and Household Tax Masters Acquisition Corporation	*****
11	Statement Regarding Computation of Per Share Earnings	None
13	Annual Report to Security Holders	None
18	Letter Regarding Change in Accounting Principles	None
19	Report furnished to Security Holders	None
21	Subsidiaries of the Registrant	21
22	Published Report Regarding Matters Submitted to Vote of Security Holders	None
23.1	Consent of Ernst & Young LLP	23.1
23.2	Statement regarding consent of Arthur Andersen LLP	23.2
24	Power of Attorney	None
31.1	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer	31.1
31.2	Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer	31.2
32	Section 1350 Certifications of Chief Executive Officer and Chief Financial Officer	32

* Filed as an exhibit to Imperial's Registration Statement on Form S-1 (File No. 33-96518) filed with the Commission on September 1, 1995, pursuant to Section 5 of the Securities Act of 1933.

** Filed as an exhibit to the Company's Registration Statement on Form S-4 (File No. 333-03551) filed with the Commission on May 10, 1996, pursuant to Section 5 of the Securities Act of 1933.*** Filed

as an exhibit to
the Company's
Form 10-K for
the year ended
December 31,
1999 (File
No. 0-26960).**** Filed

as an exhibit to
the Company's
Registrant's
Form 10-K for
the year ended
December 31,
2000 (File
No. 0-26960).***** Filed

as an exhibit to
the Company's
Registrant's
Form 10-K for
the year ended
December 31,
2001 (File
No. 0-26960).***** Filed

as an exhibit to
the Company's
Quarterly
Report on
Form 10-Q for
the quarter
ended
September 30,
2000 (File
No. 0-26960).***** Filed

as an appendix
to the
Company's
definitive proxy
materials filed
on
September 29,
2001.***** Filed

as an exhibit to
the Current
Report on
Form 8-K filed
by the Company
on February 5,
2003 (File
No. 0-26960).
Portions of this
exhibit have
been omitted
pursuant to a
request for
confidential
treatment
granted by the
Commission.

Table of Contents

***** Filed as an exhibit to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2003 (File No. 0-26960).

(b) Reports on Form 8-K. Set forth below is a description of the Current Reports on Form 8-K that we furnished during the quarter ended December 31, 2003:

On October 29, 2003, we furnished a Current Report on Form 8-K disclosing under Item 9 material prepared for presentation at an industry conference.

On November 3, 2003, we furnished a Current Report on Form 8-K disclosing under Item 12 the issuance of our press release announcing our 2003 third quarter earnings.

On November 5, 2003, we furnished a Current Report on Form 8-K disclosing under Item 9 material prepared for presentation at an industry conference.

On December 1, 2003, we furnished a Current Report on Form 8-K disclosing under Item 9 material prepared for presentation at an industry conference.

Table of Contents**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) 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.

ITLA CAPITAL CORPORATION

Date: March 15, 2004

By: /s/ George W. Haligowski

George W. Haligowski
Chairman of the Board, President
and Chief Executive Officer
(Duly Authorized Representative)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

Signature	Title	Date
<u>/s/ George W. Haligowski</u> George W. Haligowski	Chairman of the Board, President and Chief Executive Officer (<i>Principal Executive Officer</i>)	March 15, 2004
<u>/s/ Timothy M. Doyle</u> Timothy M. Doyle	Senior Managing Director and Chief Financial Officer (<i>Principal Financial and Accounting Officer</i>)	March 15, 2004
<u>/s/ Norval L. Bruce</u> Norval L. Bruce	Director	March 15, 2004
<u>/s/ Jeffrey L. Lipscomb</u> Jeffrey L. Lipscomb	Director	March 15, 2004
<u>/s/ Sandor X. Mayuga</u> Sandor X. Mayuga	Director	March 15, 2004
<u>/s/ Robert R. Reed</u> Robert R. Reed	Director	March 15, 2004
<u>/s/ Hirotaka Oribe</u> Hirotaka Oribe	Director	March 15, 2004
<u>/s/ Preston Martin</u> Preston Martin	Director	March 15, 2004

