

ITLA CAPITAL CORP  
Form 10-Q  
May 10, 2004

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

**FORM 10-Q**

(Mark One)

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

For the Quarterly Period Ended March 31, 2004

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**

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(Exact Name of Registrant as Specified in its Charter)

Delaware

95-4596322

\_\_\_\_\_  
(State or Other Jurisdiction of Incorporation or Organization)

\_\_\_\_\_  
(IRS Employer Identification No.)

888 Prospect St., Suite 110, La Jolla, California

92037

\_\_\_\_\_  
(Address of Principal Executive Offices)

\_\_\_\_\_  
(Zip Code)

(858) 551-0511

\_\_\_\_\_  
(Registrant's Telephone Number, Including Area Code)

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

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

Number of shares of common stock of the registrant: 6,255,769 outstanding as of May 3, 2004.

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**ITLA CAPITAL CORPORATION**  
**FORM 10-Q**  
**FOR THE THREE MONTHS ENDED MARCH 31, 2004**

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**Forward Looking Statements**

Safe Harbor statement under the Private Securities Litigation Reform Act of 1995: This Form 10-Q 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 portfolio 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.

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**ITLA CAPITAL CORPORATION AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS**

	March 31, 2004 (unaudited)	December 31, 2003
(in thousands except share amounts)		
<b>Assets</b>		
Cash and cash equivalents	\$ 285,441	\$ 178,318
Investment securities available for sale, at fair value	49,594	53,093
Stock in Federal Home Loan Bank	18,262	17,966
Loans, net (net of allowance for loan losses of \$33,057 and \$31,573 as of March 31, 2004 and December 31, 2003, respectively)	1,452,676	1,436,849
Real estate loans held in trust, net (net of allowance for loan losses of \$1,828 as of March 31, 2004 and December 31, 2003)	55,604	68,575
Loans held for sale	9,309	
Interest receivable	8,581	8,958
Other real estate owned, net	5,261	7,048
Premises and equipment, net	5,827	5,766
Deferred income taxes	11,532	11,609
Goodwill	3,118	3,118
Other assets	30,147	26,915
	<u>          </u>	<u>          </u>
Total assets	\$ 1,935,352	\$ 1,818,215
	<u>          </u>	<u>          </u>
<b>Liabilities and Shareholders Equity</b>		
Liabilities:		
Deposit accounts	\$ 1,222,089	\$ 1,147,017
Federal Home Loan Bank advances	298,135	362,135
Collateralized mortgage obligations	3,175	15,868
Accounts payable and other liabilities	125,846	19,696
Junior subordinated debentures	86,600	86,600
	<u>          </u>	<u>          </u>
Total liabilities	1,735,845	1,631,316
	<u>          </u>	<u>          </u>
Commitments and contingencies		
Shareholders equity:		
Preferred stock, 5,000,000 shares authorized, none issued		
Contributed capital common stock, \$.01 par value; 20,000,000 shares authorized, 8,506,205 and 8,447,294 issued as of March 31, 2004 and December 31, 2003, respectively	62,752	61,704
Retained earnings	179,191	165,407
Accumulated other comprehensive income, net	272	155
	<u>          </u>	<u>          </u>
	242,215	227,266
Less treasury stock, at cost 2,524,789 and 2,475,689 shares as of March 31, 2004 and December 31, 2003, respectively	(42,708)	(40,367)
	<u>          </u>	<u>          </u>
Total shareholders equity	199,507	186,899
	<u>          </u>	<u>          </u>

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Total liabilities and shareholders' equity	\$1,935,352	\$1,818,215
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See accompanying notes to the unaudited consolidated financial statements.

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**ITLA CAPITAL CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF INCOME**  
(Unaudited)

	<b>For the Three Months Ended March 31,</b>	
	<b>(in thousands except per share amounts)</b>	
	<b>2004</b>	<b>2003</b>
<b>Interest income:</b>		
Loans, including fees	\$ 28,914	\$ 28,614
Real estate loans held in trust	726	2,173
Cash and investment securities	2,443	2,737
<b>Total interest income</b>	<b>32,083</b>	<b>33,524</b>
<b>Interest expense:</b>		
Deposit accounts	6,514	6,848
Federal Home Loan Bank advances	1,081	1,195
Collateralized mortgage obligations	62	390
Junior subordinated debentures	1,489	—
<b>Total interest expense</b>	<b>9,146</b>	<b>8,433</b>
Net interest income before provision for loan losses	22,937	25,091
Provision for loan losses	1,400	4,500
Net interest income after provision for loan losses	21,537	20,591
<b>Non-interest income:</b>		
Premium on sale of loans, net	9,024	8,718
Late and collection fees	101	67
Other	4,269	3,751
<b>Total non-interest income</b>	<b>13,394</b>	<b>12,536</b>
<b>Non-interest expense:</b>		
Compensation and benefits	6,156	5,352
Occupancy and equipment	1,328	1,076
Other	3,868	3,689
<b>Total general and administrative</b>	<b>11,352</b>	<b>10,117</b>
Real estate owned expense, net	96	142
Provision for losses on other real estate owned	1,000	330
Gain on sale of other real estate owned, net	(39)	(329)
<b>Total real estate owned expense, net</b>	<b>1,057</b>	<b>143</b>
<b>Total non-interest expense</b>	<b>12,409</b>	<b>10,260</b>

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Income before provision for income taxes and minority interest in income of subsidiary	22,522	22,867
Minority interest in income of subsidiary		1,520
	<u>          </u>	<u>          </u>
Income before provision for income taxes	22,522	21,347
Provision for income taxes	8,738	8,326
	<u>          </u>	<u>          </u>
NET INCOME	\$ 13,784	\$ 13,021
	<u>          </u>	<u>          </u>
BASIC EARNINGS PER SHARE	\$ 2.21	\$ 2.17
	<u>          </u>	<u>          </u>
DILUTED EARNINGS PER SHARE	\$ 2.07	\$ 2.02
	<u>          </u>	<u>          </u>

See accompanying notes to the unaudited consolidated financial statements.



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**ITLA CAPITAL CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(Unaudited)**

	<b>For the Three Months Ended March 31,</b>	
	<b>2004</b>	<b>2003</b>
	<b>(in thousands)</b>	
<b>Cash Flows From Operating Activities:</b>		
Net Income	\$ 13,784	\$ 13,021
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of premises and equipment	477	388
Amortization of premium on purchased loans	692	505
Accretion of deferred loan origination fees, net of costs	(628)	(839)
Provision for loan losses	1,400	4,500
Provision for losses on other real estate owned	1,000	330
Premium on sale of RAL loans, net	(9,024)	(8,718)
Other, net	(25)	1
Decrease in interest receivable	377	5
Increase in other assets	(3,298)	(9,566)
Increase in accounts payable and other liabilities	106,150	54,011
	<b>110,905</b>	<b>53,638</b>
<b>Cash Flows From Investing Activities:</b>		
Purchases of investment securities available for sale		(18,149)
Proceeds from the maturity and calls of investment securities available for sale	3,633	12,941
Purchase of stock in Federal Home Loan Bank	(138)	(222)
Purchase of loans		(1,914)
Origination of RAL loans	(12,800,573)	(11,585,047)
Proceeds from the participation in RAL loans	12,797,195	11,584,877
(Increase) decrease in loans, net	(14,644)	50,740
Repayment of real estate loans held in trust	12,505	6,922
Proceeds from sale of other real estate owned	1,738	4,742
Other investing activities, net	(538)	(569)
	<b>(822)</b>	<b>54,321</b>
<b>Cash Flows From Financing Activities:</b>		
Proceeds from exercise of employee stock options	1,004	8
Cash paid to acquire treasury stock	(2,341)	
Principal payments on collateralized mortgage obligations	(12,695)	(7,316)
Increase in deposit accounts	75,072	3,603
Net repayments of short-term borrowings from the Federal Home Loan Bank	(41,000)	(187,000)
Proceeds from long-term borrowings from the Federal Home Loan Bank	10,000	16,000
Repayments from long-term borrowings from the Federal Home Loan Bank	(33,000)	(1,700)
	<b>(2,960)</b>	<b>(176,405)</b>
Net increase (decrease) in cash and cash equivalents	107,123	(68,446)
Cash and cash equivalents at beginning of period	178,318	160,848
	<b>\$ 285,441</b>	<b>\$ 92,402</b>
Cash and cash equivalents at end of period		

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	<u>          </u>	<u>          </u>
Supplemental Cash Flow Information:		
Cash paid during the period for interest	\$ 9,476	\$ 8,028
Cash paid during the period for income taxes	\$	\$ 5,010
Non-cash Investing Transactions:		
Loans transferred to other real estate owned	\$ 912	\$ 3,012

See accompanying notes to the unaudited consolidated financial statements.

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**ITLA CAPITAL CORPORATION AND SUBSIDIARIES**

**NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 BASIS OF PRESENTATION**

The unaudited consolidated financial statements of ITLA Capital Corporation (the Company) included herein reflect all normal recurring adjustments which are, in the opinion of management, necessary to present fairly the results of operations and financial position of the Company, as of and for the interim periods indicated. The unaudited consolidated financial statements include the accounts of ITLA Capital Corporation and its wholly-owned subsidiaries, Imperial Capital Bank (the Bank), and Imperial Capital Real Estate Investment Trust (Imperial Capital REIT).

On December 31, 2003, the Company adopted FASB Interpretation No. 46 (FIN 46), Consolidation of Variable Interest Entities, which addresses consolidation by business enterprises of variable interest entities having certain characteristics. In connection with the Company's adoption of FIN 46, ITLA Capital Statutory Trust I (Trust I), ITLA Capital Statutory Trust II (Trust II), ITLA Capital Statutory Trust III (Trust III), ITLA Capital Statutory Trust IV (Trust IV), and ITLA Capital Statutory Trust V (Trust V), collectively referred to as the Trusts, were not consolidated as of December 31, 2003. The result of the deconsolidation was to recognize the Company's investment 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, effective January 1, 2004, the Company recognized interest expense on the subordinated debentures in the consolidated statements of income. Prior to FIN 46, the Company consolidated the Trusts and reported the trust preferred securities issued by the Trusts 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. The trust preferred securities currently 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 proposed a rule on May 6, 2004 related to the qualification of the trust preferred securities as Tier 1 capital. Under the proposed rule, the Company's trust preferred securities would still qualify as Tier 1 capital. As of March 31, 2004, the Company would meet all requirements to maintain its well capitalized designation under applicable regulatory guidelines regardless of the inclusion of the trust preferred securities in Tier 1 capital. Financial information prior to the adoption of FIN 46 has not been restated.

All intercompany transactions and balances have been eliminated. Certain information and disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to the rules and regulations of the U.S. Securities and Exchange Commission. Certain amounts in prior periods have been reclassified to conform to the presentation in the current period. The results of operations for the three months ended March 31, 2004 are not necessarily indicative of the results of operations for the remainder of the year.

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These unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in our annual report on Form 10-K for the year ended December 31, 2003.

**NOTE 2 ACCOUNTING FOR STOCK-BASED COMPENSATION**

The Company has stock-based compensation plans. These plans are accounted for under APB Opinion No. 25, Accounting for Stock Issued to Employees, and accordingly, no compensation costs have been recognized in the accompanying unaudited consolidated statements of income. The Company applies Statement of Financial Accounting Standards ( SFAS ) No. 123, Accounting for Stock-Based Compensation, for disclosure purposes only. SFAS No. 123 disclosures include pro forma net income and earning per share as if compensation expense had been recognized using the fair value of the options at the date of grant. 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:

	<b>For the Three Months Ended March 31,</b>	
	<b>2004</b>	<b>2003</b>
	(in thousands, except per share data)	
Net income, as reported	\$ 13,784	\$ 13,021
Less: Stock-based employee compensation expense determined under the fair value method, net of tax	337	341
<b>Pro forma net income</b>	<b>\$ 13,447</b>	<b>\$ 12,680</b>
<b>Earnings per share:</b>		
Basic as reported	\$ 2.21	\$ 2.17
Basic pro forma	\$ 2.15	\$ 2.11
Diluted as reported	\$ 2.07	\$ 2.02
Diluted pro forma	\$ 2.02	\$ 1.97

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:

	<b>Weighted-Average Assumptions for Option Grants</b>	
	<b>2004</b>	<b>2003</b>
Dividend Yield	0.00%	0.00%
Expected Volatility	38.04%	31.36%
Risk-Free Interest Rates	3.65%-4.34%	4.62%-4.88%
Expected Lives	Seven Years	Seven Years
Weighted-Average Fair Value	12.37	11.36

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**NOTE 3 EARNINGS PER SHARE**

Basic Earnings Per Share ( Basic EPS ) is computed by dividing net income by the weighted-average number of common shares outstanding for the period. Diluted Earnings Per Share ( Diluted EPS ) reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock which shared in the Company's earnings.

The following is a reconciliation of the calculation of Basic EPS and Diluted EPS:

		<b>For the Three Months Ended March 31,</b>		
		<b>Net Income</b>	<b>Weighted- Average Shares Outstanding</b>	<b>Per Share Amount</b>
(in thousands, except per share data)				
<b>2004</b>	Basic EPS	\$ 13,784	6,240	\$