ITLA CAPITAL CORP
Form 10-K
March 15, 2004

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

FORM 10-K

(Mark One)

[X] **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	**95-4596322**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
888 Prospect Street, Suite 110, La Jolla, California	**92037**
(Address of Principal Executive Offices)	(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 [X] 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 [X] 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

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.)

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FOR THE FISCAL YEAR ENDED DECEMBER 31, 2003

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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.

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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

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

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

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

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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

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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.

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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

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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.

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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.

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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.

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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.

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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%.

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

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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.

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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.

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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			
	High	**Low**	**Close**	**Average Daily Closing Price**
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				

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

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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					

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
Total Assets	$1,818,215	$1,721,965	$1,508,308	$1,415,143	$1,115,823
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
Total Liabilities and Shareholders Equity	$1,818,215	$1,721,965	$1,508,308	$1,415,143	$1,115,823
Book value per share	$ 31.30	$ 27.11	$ 23.54	$ 20.05	$ 17.22

(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

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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 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 polices 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 polices 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.

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.

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.

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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 *(1)*	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 *(1)*	97,698	5,980	6.12%	143,705	10,239	7.13%	189,349	14,954	7.90%
Franchise loans *(1)*	66,101	4,772	7.22%	60,492	4,479	7.40%	32,956	2,716	8.24%
Motion picture financing *(1)*	99,104	7,433	7.50%	18,060	1,349	7.47%			
Commercial and other loans *(1)*	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%

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.

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 loans 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.

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.

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

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.

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.

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.