IRWIN FINANCIAL CORP
Form 10-Q
October 31, 2007

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2007

o **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: 0-6835
IRWIN FINANCIAL CORPORATION
(Exact Name of Corporation as Specified in its Charter)

Indiana	**35-1286807**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
500 Washington Street Columbus, Indiana	**47201**
(Address of Principal Executive Offices)	(Zip Code)
(812) 376-1909	**www.irwinfinancial.com**
(Corporation s Telephone Number, Including Area Code)	(Web Site)

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.
þ Yes o No

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act (Check one):
Large accelerated filer o Accelerated filer þ Non-accelerated filer o

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

As of October 26, 2007, there were outstanding 29,349,108 common shares, no par value, of the Registrant.

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PART I. FINANCIAL INFORMATION.

Item 1. Financial Statements.

IRWIN FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS (Unaudited)

	September 30, 2007	December 31, 2006
	(Dollars in thousands)	
Assets:		
Cash and cash equivalents	$ 85,673	$ 145,765
Interest-bearing deposits with financial institutions	32,841	53,106
Residual interests	11,005	10,320
Investment securities- held-to-maturity (Fair value: $17,724 at September 30, 2007 and $17,893 at December 31, 2006)	17,721	18,066
Investment securities- available-for-sale	124,069	110,364
Loans held for sale	3,253	237,510
Loans and leases, net of unearned income Note 3	5,676,690	5,238,193
Less: Allowance for loan and lease losses Note 4	(104,443)	(74,468)
	5,572,247	5,163,725
Servicing assets Note 5	25,324	31,949
Accounts receivable	45,091	208,585
Accrued interest receivable	26,295	26,470
Premises and equipment	38,604	36,211
Other assets	171,361	139,314
Assets held for sale Note 2	8,364	56,573
Total assets	$6,161,848	$6,237,958
Liabilities and Shareholders Equity:		
Deposits		
Noninterest-bearing	$ 383,142	$ 687,626
Interest-bearing	2,348,819	1,756,109
Certificates of deposit over $100,000	771,109	1,107,781
	3,503,070	3,551,516
Short-term borrowings Note 6	539,273	602,443
Collateralized debt Note 7	1,288,119	1,173,012
Other long-term debt	233,877	233,889
Other liabilities	108,713	146,596
Total liabilities	5,673,052	5,707,456
Commitments and contingencies Note 11		
Shareholders equity		
Preferred stock, no par value authorized 4,000,000 shares; none issued		
Noncumulative perpetual preferred stock 15,000 shares authorized and issued	14,441	14,518
	116,292	116,192

Common stock, no par value authorized 40,000,000 shares; issued 29,900,305 shares and 29,879,773 shares as of September 30, 2007 and December 31, 2006; 701,751 shares 143,543 shares in treasury as of September 30, 2007 and December 31, 2006		
Additional paid-in capital	2,772	1,583
Accumulated other comprehensive income (loss), net of deferred income tax benefit of $5,113 and $4,813 as of September 30, 2007 and December 31, 2006	1,332	(4,364)
Retained earnings	367,483	405,835
	502,320	533,764
Less treasury stock, at cost	(13,524)	(3,262)
Total shareholders equity	488,796	530,502
Total liabilities and shareholders equity	$6,161,848	$6,237,958

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

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IRWIN FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

	For the Three Months Ended September 30,	
	2007	2006
	(Dollars in thousands, except per share)	
Interest income:		
Loans and leases	$ 126,180	$ 113,923
Loans held for sale	585	7,075
Residual interests	268	279
Investment securities	2,738	2,422
Federal funds sold	79	89
Total interest income	129,850	123,788
Interest expense:		
Deposits	34,747	34,322
Short-term borrowings	7,436	4,344
Collateralized debt	18,563	14,305
Other long-term debt	3,958	5,520
Total interest expense	64,704	58,491
Net interest income	65,146	65,297
Provision for loan and lease losses Note 4	28,493	9,135
Net interest income after provision for loan and lease losses	36,653	56,162
Other income:		
Loan servicing fees	4,415	6,207
Amortization and impairment of servicing assets	(2,686)	(5,343)
Gain from sales of loans and loans held for sale	3,329	1,640
Trading gains	876	968
Derivative losses, net	(5,673)	(2,301)
Other	6,771	6,176
	7,032	7,347
Other expense:		
Salaries	24,043	23,815
Pension and other employee benefits	6,478	6,586
Office expense	2,126	2,413
Premises and equipment	5,500	5,040
Marketing and development	1,354	614
Professional fees	2,086	2,479
Other	4,758	9,917
	46,345	50,864

(Loss) income before income taxes from continuing operations		(2,660)		12,645
(Benefit) provision for income taxes		(1,857)		3,550
Net (loss) income from continuing operations		(803)		9,095
Loss from discontinued operations, net of $11,540 and $8,884 income tax benefit, respectively Note 2		(17,227)		(13,302)
Net loss	$	(18,030)	$	(4,207)
Earnings per share from continuing operations: Note 9				
Basic	$	(0.04)	$	0.31
Diluted	$	(0.05)	$	0.30
Earnings per share: Note 9				
Basic	$	(0.63)	$	(0.14)
Diluted	$	(0.64)	$	(0.14)
Dividends per share	$	0.12	$	0.11

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

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IRWIN FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

	For the Nine Months Ended September 30,	
	2007	2006
	(Dollars in thousands, except per share)	
Interest income:		
Loans and leases	$ 369,727	$ 316,904
Loans held for sale	6,663	28,285
Residual interests	817	1,409
Investment securities	7,757	6,128
Federal funds sold	602	138
Total interest income	385,566	352,864
Interest expense:		
Deposits	103,178	98,621
Short-term borrowings	22,054	11,843
Collateralized debt	51,491	37,013
Other long-term debt	11,726	14,641
Total interest expense	188,449	162,118
Net interest income	197,117	190,746
Provision for loan and lease losses Note 4	71,155	25,154
Net interest income after provision for loan and lease losses	125,962	165,592
Other income:		
Loan servicing fees	15,443	25,164
Amortization and impairment of servicing assets	(9,924)	(16,888)
Gain from sales of loans and loans held for sale	690	816
Trading gains	868	751
Derivative (losses) gains, net	(10,014)	1,138
Other	18,736	19,408
	15,799	30,389
Other expense:		
Salaries	73,688	73,958
Pension and other employee benefits	20,912	21,985
Office expense	7,002	6,698
Premises and equipment	16,468	15,513
Marketing and development	3,931	2,004
Professional fees	6,853	7,346
Other	16,839	27,468
	145,693	154,972

(Loss) income before income taxes from continuing operations		(3,932)		41,009
(Benefit) provision for income taxes		(2,507)		14,255
Net (loss) income from continuing operations		(1,425)		26,754
Loss from discontinued operations, net of $18,250 and $19,964 income tax benefit, respectively Note 2		(27,123)		(29,948)
Net loss	$	(28,548)	$	(3,194)
Earnings per share from continuing operations: Note 9				
Basic	$	(0.08)	$	0.91
Diluted	$	(0.11)	$	0.90
Earnings per share: Note 9				
Basic	$	(1.01)	$	(0.11)
Diluted	$	(1.03)	$	(0.12)
Dividends per share	$	0.36	$	0.33

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

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IRWIN FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY (Unaudited)
For the Nine Months Ended September 30, 2007, and 2006

			Accumulated Other Comprehensive Income							
				Unrealized Gain/Loss						
	Total	Retained Earnings	Foreign Currency	Securities	Derivatives	Defined Benefit Plans	Additional Paid in Capital	Common Stock	Treasury Stock	Perpetual Preferred Stock
	(Dollars in thousands)									
Balance at January 1, 2007	$530,502	$405,835	$2,884	$(344)	$ (30)	$(6,874)	$1,583	$116,192	$ (3,262)	$14,518
Net loss	(28,548)	(28,548)								
Unrealized loss on investment securities net of $300 tax benefit	(450)			(450)						
Unrealized loss on derivatives net of $318 tax benefit	(477)				(477)					
Foreign currency adjustment	6,623		6,623							
Other comprehensive income	5,696									
Total comprehensive income	(22,852)									
Cash dividends common stock	(10,543)	(10,543)								
Cash dividends preferred stock	(1,004)	(1,004)								
FAS 156 adoption	1,743	1,743								
Tax benefit on stock option exercises	91						91			
Stock compensation expense	1,296						1,296			
Stock issuance costs	(77)									(77)
Stock:										

Purchase of 671,186 shares	(12,781)								(12,781)	
Sales of 117,715 shares	2,421						(198)	100	2,519	
Balance at September 30, 2007	$488,796	$367,483	$9,507	$(794)	$(507)	$(6,874)	$2,772	$116,292	$(13,524)	$14,441
Balance at January 1, 2006	$512,334	$418,784	$3,341	$(373)	$ 754	$ (274)	$ 50	$112,000	$(21,948)	$
Net loss	(3,194)	(3,194)								
Unrealized loss on investment securities net of $50 tax benefit	(75)			(75)						
Unrealized loss on derivative net of $250 tax benefit	(375)				(375)					
Foreign currency adjustment	972		972							
Other comprehensive income	522									
Total comprehensive income	(2,672)									
Cash dividends	(9,818)	(9,818)								
Tax benefit on stock option exercises	349						349			
Stock compensation expense	1,419						1,419			
Conversion of trust preferred shares to 1,013,938 shares of common stock	19,513	(1,058)						1,070	19,501	
Stock:										
Purchase of 52,230 shares	(1,027)								(1,027)	
Sales of 187,301 shares	2,957	(508)					(476)	1,153	2,788	

Balance at September 30, 2006	$523,055	$404,206	$4,313	$(448)	$ 379	$ (274)	$1,342	$114,223	$ (686)	$

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

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IRWIN FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	For the Nine Months ended September 30,	
	2007	2006
	(Dollars in thousands)	
(Loss) Income from continuing operations	$ (1,425)	$ 26,754
Loss from discontinued operations	(27,123)	(29,948)
Net loss	(28,548)	(3,194)
Adjustments to reconcile net loss to cash provided by operating activities:		
Depreciation, amortization, and accretion, net	7,742	6,071
Amortization and impairment of servicing assets	10,174	57,878
Provision for loan and lease losses	71,155	25,183
Loss on sale of mortgage servicing assets		15,829
Loss (gain) from sales of loans held for sale	11,279	(44,237)
Originations and purchases of loans held for sale	(497,707)	(6,969,021)
Proceeds from sales and repayments of loans held for sale	555,820	8,014,813
Proceeds from the sale of mortgage servicing assets	137	79,395
Net decrease in residuals	132	13,181
Net decrease in accounts receivable	163,494	65,540
Other, net	(65,082)	(139,727)
Net cash provided by operating activities	228,596	1,121,711
Investing activities:		
Proceeds from maturities/calls of investment securities:		
Held-to-maturity	2,438	1,055
Available-for-sale	2,818	9,015
Purchase of investment securities:		
Held-to-maturity	(2,167)	(2,648)
Available-for-sale	(17,316)	(23,006)
Net decrease in interest-bearing deposits	20,265	396
Net increase in loans, excluding sales	(337,626)	(677,505)
Proceeds from sale of loans	66,748	46,728
Other, net	(7,739)	(9,663)
Net cash used by investing activities	(272,579)	(655,628)
Financing activities:		
Net decrease in deposits	(48,445)	(108,793)
Net decrease in short-term borrowings	(63,170)	(733,205)
Proceeds from issuance of collateralized debt	364,579	650,808
Repayments of collateralized debt	(249,514)	(276,832)
Proceeds from the issuance of trust preferred securities		31,500
Repayments of long term debt	(11)	(47,583)
Purchase of treasury stock for employee benefit plans	(12,781)	(1,027)

Proceeds from sale of stock for employee benefit plans		2,512		4,053
Dividends paid		(11,547)		(9,818)
Net cash used by financing activities		(18,377)		(490,897)
Effect of exchange rate changes on cash		2,268		505
Net decrease in cash and cash equivalents		(60,092)		(24,309)
Cash and cash equivalents at beginning of period		145,765		155,486
Cash and cash equivalents at end of period	$	85,673	$	131,177
Supplemental disclosures of cash flow information:				
Cash flow during the period:				
Interest paid	$	187,623	$	178,360
Income taxes paid	$	12,001	$	35,150
Noncash transactions:				
Adoption of FAS 156	$	2,905	$	
Loans transferred from held-for-sale to held-for-investment	$	196,423	$	
Other real estate owned	$	12,729	$	6,805
Conversion of trust preferred stock to common stock	$		$	19,513

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

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 Accounting Policies, Management Judgments and Accounting Estimates

Consolidation: Irwin Financial Corporation and its subsidiaries (the Corporation) provide financial services throughout the United States (U.S.) and Canada. We are engaged in commercial banking, commercial finance and home equity lending. We are in the process of exiting the mortgage banking segment. Our direct and indirect subsidiaries include, Irwin Union Bank and Trust Company, Irwin Union Bank, F.S.B., Irwin Commercial Finance Corporation, Irwin Home Equity Corporation and Irwin Mortgage Corporation (IMC). Intercompany balances and transactions have been eliminated in consolidation. In the opinion of management, the financial statements reflect all material adjustments necessary for a fair presentation. The Corporation does not meet the criteria as primary beneficiary for our wholly-owned trusts holding our company-obligated mandatorily redeemable preferred securities established by Financial Accounting Standards Board (FASB) Interpretation No. 46 (FIN 46), Consolidation of Variable Interest Entities. As a result, these trusts are not consolidated.

Because we are in the process of exiting the mortgage banking line of business, the financial statements and footnotes within this report conform to the presentation required in Statement of Financial Accounting Standard (SFAS) 144, Accounting for the Impairment or Disposal of Long-Lived Assets. Certain of the balance sheet assets related to this line of business are being reported as assets held for sale. See Note 2 for additional information.

Use of Estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents Defined: For purposes of the statement of cash flows, we consider cash and due from banks to be cash equivalents.

Allowance for Loan and Lease Losses: The allowance for loan and lease losses is an estimate based on management s judgment applying the principles of SFAS 5, Accounting for Contingencies, SFAS 114, Accounting by Creditors for Impairment of a Loan, and SFAS 118, Accounting by Creditors for Impairment of a Loan Income Recognition and Disclosures. The allowance is maintained at a level we believe is adequate to absorb probable losses inherent in the loan and lease portfolio. We perform an assessment of the adequacy of the allowance on a quarterly basis.

Within the allowance, there are specific and expected loss components. The specific loss component is assessed for loans we believe to be impaired in accordance with SFAS 114. We have defined impairment as nonaccrual loans. For loans determined to be impaired, we measure the level of impairment by comparing the loan s carrying value to fair value using one of the following fair value measurement techniques: present value of expected future cash flows, observable market price, or fair value of the associated collateral. An allowance is established when the fair value implies a value that is lower than the carrying value of that loan. In addition to establishing allowance levels for specifically identified impaired loans, management determines an allowance for all other loans in the portfolio for which historical experience indicates that certain losses exist. These loans are segregated by major product type, and in some instances, by aging, with an estimated loss ratio applied against each product type and aging category. The loss ratio is generally based upon historic loss experience for each loan type as adjusted for certain environmental factors management believes to be relevant.

It is our policy to promptly charge off any loan, or portion thereof, which is deemed to be uncollectible. This includes, but is not limited to, any loan rated Loss by the regulatory authorities. Impaired commercial credits are considered on a case-by-case basis. The amount charged off includes any accrued interest. Unless there is a significant reason to the contrary, consumer loans are charged off when deemed uncollectible, but generally no later than when a loan is past due 180 days.

Servicing Assets: When we securitize or sell loans, we may retain the right to service the underlying loans sold. For cases in which we retain servicing rights, a portion of the cost basis of loans sold is allocated to a servicing asset based on its fair value relative to the loans sold and the servicing asset combined. Prior to the January 1, 2007, all servicing rights were carried at lower of cost or fair market value. We use a combination of observed pricing on similar,

market-traded servicing rights and internal valuation models that

calculate the present value of future cash flows to determine the fair value of the servicing assets. These models are supplemented and calibrated to market prices using inputs from independent servicing brokers, industry surveys and valuation experts. In using this valuation method, we incorporate assumptions that we believe market participants would use in estimating future net servicing income, which include, among other items, estimates of the cost of servicing per loan, the discount rate, float value, an inflation rate, ancillary income per loan, prepayment speeds, and default rates. Due to the disruption of the residential mortgage market in the third quarter of 2007 and based on the advice of third-party experts, we decreased future prepayment assumptions to align with recent borrower behavior. Prior to January 1, 2007, all servicing assets were amortized over the period of and in proportion to estimated net servicing income.

For servicing assets associated with second mortgages and high loan-to-value first mortgages, the fair value measurement method of reporting these servicing rights was elected beginning January 1, 2007, in accordance with SFAS 156, Accounting for Servicing of Financial Assets. Under the fair value method, we measure servicing assets at fair value at each reporting date and report changes in fair value in earnings in the period in which the changes occur. All remaining servicing rights follow the amortization method for subsequent measurement whereby these servicing rights are amortized in proportion to and over the period of estimated net servicing income.

Incentive Servicing Fees: For whole loan sales of certain home equity loans, in addition to our normal servicing fee, we have the right to an incentive servicing fee (ISF) that will provide cash payments to us if a pre-established return for the certificate holders and certain structure-specific loan credit and servicing performance metrics are met. Generally the structure-specific metrics involve both a delinquency and a loss test. The delinquency test is satisfied if, as of the last business day of the preceding month, delinquencies on the current pool of mortgage loans are less than or equal to a given percentage. The loss test is satisfied if, on the last business day of the preceding month, the percentage of cumulative losses on the original pool of mortgage loans is less than or equal to the applicable percentage as outlined in the specific deal documents. We receive ISF payments monthly, once the pre-established return has been paid to the certificate holder, if the delinquency and loss percentages are within guidelines. If we are terminated or replaced for cause as servicer under the securitization, the cash flow stream under the ISF contract terminates.

We account for ISFs similar to management contracts under Emerging Issues Task Force Topic No. D-96, Accounting for Management Fees Based on a Formula. Accordingly, we recognize revenue on a cash basis as the pre-established performance metrics are met and cash is due.

Income Taxes: A consolidated tax return is filed for all eligible entities. In accordance with SFAS 109, deferred income taxes are computed using the liability method, which establishes a deferred tax asset or liability based on temporary differences between the tax basis of an asset or liability and the basis recorded in the financial statements.

Recent Accounting Developments: In March 2006, the FASB issued SFAS 156, Accounting for Servicing of Financial Assets, an amendment of FASB Statement No. 140. This statement requires that all separately recognized servicing assets and servicing liabilities be initially measured at fair value, if practicable. The statement permits, but does not require, the subsequent measurement of classes of servicing assets and servicing liabilities at fair value, to better align with the use of derivatives used to mitigate the inherent risks of these assets and liabilities. Offsetting changes in fair value are recognized through income. This statement is effective as of January 1, 2007. We elected the fair value treatment for servicing rights associated with second mortgage and high loan-to-value first mortgage loans at our home equity lending line of business. Implementation of the fair value treatment under SFAS 156 resulted in a one-time increase to retained earnings of $1.7 million. This represents the after-tax effect of the $2.9 million fair value adjustment to the mortgage servicing asset as of January 1, 2007.

In September 2006, the FASB issued SFAS 157, Fair Value Measurements. This statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We are currently evaluating this new statement and have not yet determined the ultimate impact it will have on our financial statements.

In February 2007, the FASB issued SFAS 159, The Fair Value Option for Financial Assets and Financial Liabilities. This statement permits entities to choose to measure certain financial instruments at fair value. This

statement is effective for financial statements issued for fiscal years beginning after November 15, 2007. Early adoption is permitted as of January 1, 2007. We elected

not to early adopt this statement. We are currently evaluating this new statement and have not yet determined the ultimate impact it will have on our financial statements once it becomes effective in 2008.

Effective January 1, 2007, we adopted FASB Interpretation Number 48, Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109, (FIN No. 48), which prescribes a single, comprehensive model for how a company should recognize, measure, present and disclose in its financial statements uncertain tax positions that the company has taken or expects to take on its tax returns. Upon adoption of FIN No. 48, we did not recognize any material adjustment in our liability for unrecognized tax benefits. As of January 1, 2007, our unrecognized tax benefits were $10.7 million, $0.7 million of which would, if recognized, favorably affect the effective tax rate in future periods. As of September 30, 2007, our unrecognized tax benefits were $13.4 million, $0.4 million of which would, if recognized, favorably affect the effective tax rate in future periods.

Our continuing practice is to recognize potential interest and penalties related to unrecognized tax benefits in income tax expense. As of January 1, 2007, we had approximately $0.8 million accrued for interest and no accrual for penalties related to unrecognized tax benefits. As of September 30, 2007, we have approximately $1.0 million accrued for interest related to unrecognized tax benefits and no accrual for penalties.

Tax years 2004-2006 remain open to examination by major taxing jurisdictions. Certain state tax returns remain open to examination for tax years 2003-2006.

Reclassifications: Certain amounts in the 2006 consolidated financial statements have been reclassified to conform to the 2007 presentation. These changes had no impact on previously reported net income or shareholders equity.

Note 2 Discontinued Operations

In 2006, we sold to five separate buyers the mortgage banking line of business origination operation, including the majority of this segment s loans held for sale, as well as the majority of this segment s capitalized mortgage servicing rights. In January 2007, we transferred a nominal amount of assets associated with this segment s servicing platform (but not mortgage servicing rights) to a sixth buyer. The majority of the cash proceeds from the sales have been collected. We have staff continuing to work at this discontinued operation through the wind-down of its remaining assets, such as repurchased loans.

In accordance with the provisions of SFAS 144, the results of operations of the mortgage banking line of business for the current and prior periods have been reported as discontinued operations. In addition, certain of the remaining assets for this segment have been reclassified as held for sale on the consolidated balance sheet.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	**2006**	**2007**	**2006**
	(Dollars in thousands)			
Net revenues	$ (5,127)	$ 6,757	$ (13,803)	$ 36,271
Other expense	(23,640)	(28,943)	(31,570)	(86,183)
Loss before income taxes	(28,767)	(22,186)	(45,373)	(49,912)
Income taxes	11,540	8,884	18,250	19,964
Net loss from discontinued operations	$ (17,227)	$ (13,302)	$ (27,123)	$ (29,948)

	September 30, 2007	**December 31, 2006**
	(Dollars in thousands)	
Loans, net of allowance, and Loans held for sale	$ 4,227	$ 48,555
Net servicing asset		385
Other assets	4,137	7,633

Assets held for sale	$	8,364	$	56,573

Note 3 Loans and Leases

Loans and leases are summarized as follows:

	September 30, 2007	December 31, 2006
	(Dollars in thousands)	
Commercial, financial and agricultural	$2,290,394	$ 2,249,988
Residential real estate-construction	381,462	377,601
Residential real estate-mortgage	1,737,437	1,522,616
Consumer	33,085	31,581
Commercial financing		
Franchise financing	838,317	699,969
Domestic leasing	307,958	296,056
Canadian leasing	459,798	358,783
Unearned income		
Franchise financing	(270,814)	(211,480)
Domestic leasing	(43,693)	(42,782)
Canadian leasing	(57,254)	(44,139)
Total	$5,676,690	$ 5,238,193

Note 4 Allowance for Loan and Lease Losses

Changes in the allowance for loan and lease losses are summarized below:

	September 30, 2007 And the Nine Months Then Ended	December 31, 2006 And the Year Then Ended
	(Dollars in thousands)	
Balance at beginning of year	$ 74,468	$ 59,223
Provision for loan and lease losses	71,155	35,101
Charge-offs	(48,619)	(30,810)
Recoveries	7,881	11,208
Reduction due to reclassification or sale of loans	(1,006)	(246)
Foreign currency adjustment	564	(8)
Balance at end of period	$ 104,443	$ 74,468

Note 5 Servicing Assets

We adopted the fair value treatment for servicing assets associated with our second mortgage and high loan-to-value first mortgage portfolios as of January 1, 2007. The effect of remeasuring the selected servicing assets at fair value was reported as a cumulative-effect adjustment to retained earnings, increasing retained earnings $1.7 million, net of tax. Changes in fair value subsequent to adoption were recorded through amortization and impairment of servicing assets. All other first mortgage loans continue to be accounted for using the amortization method with impairment recognized. These mortgage servicing assets are recorded at lower of their allocated cost

basis or fair value and a valuation allowance is recorded for any stratum that is impaired.

We estimate the fair value of the servicing assets using a cash flow model to project future expected cash flows based upon a set of valuation assumptions we believe market participants would use for similar assets. The primary assumptions we use for valuing our mortgage servicing assets include prepayment speeds, default rates, cost to service and discount rates. We review these assumptions on a regular basis to ensure that they remain consistent with current market conditions. Additionally, we periodically receive third

party estimates of the portfolio value from independent valuation firms. Inaccurate assumptions in valuing mortgage servicing rights could adversely affect our results of operations. For servicing rights accounted for under the amortization method, we also review these mortgage servicing assets for other-than-temporary impairment each quarter and recognize a direct write-down when the recoverability of a recorded valuation allowance is determined to be remote. Unlike a valuation allowance, a direct write-down permanently reduces the unamortized cost of the mortgage servicing rights asset and the valuation allowance, precluding subsequent reversals.

Changes in our fair value servicing assets are shown below:

	September 30, 2007 And the Nine Months Then Ended	December 31, 2006 And the Year Then Ended
	(Dollars in thousands)	
Beginning balance	$ 27,725	NA
Gain from initial adoption of SFAS 156	2,905	NA
Changes in fair value:		
Due to changes in valuation inputs or assumptions (1)	(1,056)	NA
Other changes in fair value (2)	(7,920)	NA
Mortgage servicing asset from continuing operations	$ 21,654	NA

(1) Principally reflects changes in discount rates and prepayment speed assumptions, primarily due to changes in interest rates.

(2) Represents changes due to realization of expected cash flows.

Changes in our amortizing servicing assets are shown below:

	September 30, 2007 And the Nine Months Then Ended	December 31, 2006 And the Year Then Ended

	(Dollars in thousands)	
Beginning balance	$ 31,949	$ 34,445
Initial adoption of SFAS 156	(27,725)	
Additions	396	17,884
Reduction due to clean up call	(2)	
Amortization	(929)	(21,027)
(Impairment) recovery	(19)	647
Mortgage servicing asset from continuing operations	$ 3,670	$ 31,949

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We have established a valuation allowance to record amortizing servicing assets at their lower of cost or market value. Changes in the allowance are summarized below:

	September 30, 2007 And the Nine Months Then Ended	December 31, 2006 And the Year Then Ended
Balance at beginning of year	$ 483	$ 1,152
Transfer of assets from amortizing to fair value	(332)	
Impairment (recovery)	19	(647)
Reclass for sales of servicing and clean up calls		(22)
Valuation allowance from continuing operations	$ 170	$ 483

Note 6 Short-Term Borrowings

Short-term borrowings are summarized as follows:

	September 30, 2007	December 31, 2006
	(Dollars in thousands)	
Federal Home Loan Bank borrowings	$ 465,173	$ 371,693
Federal funds	74,100	230,500
Other		250
Total	$ 539,273	$ 602,443
Weighted average interest rate	4.70%	4.49%

Federal Home Loan Bank borrowings are collateralized by loans and loans held for sale.

We also have lines of credit available to fund loan originations and operations with variable rates ranging from 4.83% to 6.75% at September 30, 2007.

Note 7 Collateralized Debt

We pledge or sell loans structured as secured financings at our home equity and commercial finance lines of business. Sale treatment is precluded on these transactions because we fail the true-sale requirements of SFAS 140 as we maintain effective control over the loans and leases securitized. This type of structure results in cash being received, debt being recorded, and the establishment of an allowance for credit losses. The notes associated with these transactions are collateralized by $1.5 billion in home equity loans, home equity lines of credit, and leases. The principal and interest on these debt securities are paid using the cash flows from the underlying loans and leases. Accordingly, the timing of the principal payments on these debt securities is dependent on the payments received on the underlying collateral. The interest rates on the bonds are both fixed and floating.

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Collateralized debt is summarized as follows:

	Contractual Maturity	Weighted Average Interest Rate at September 30, 2007	September 30, 2007	December 31, 2006
			(Dollars in thousands)	
Commercial finance line of business				
Domestic asset backed note			$	$ 5,797
Canadian asset backed notes:				
Note 1	revolving	5.5	48,799	30,611
Note 2	9/2012	5.3	221,076	179,508
Note 3	10/2009	4.5	5,070	8,157
Home equity line of business				
2004-1 asset backed notes:				
Variable rate senior note	12/2024-12/2034	5.8	34,593	50,072
Variable rate subordinate note	12/2034	6.7	24,775	24,775
2005-1 asset backed notes:				
Variable rate senior note	6/2025-6/2035	5.7	24,971	40,972
Fixed rate senior note	6/2035	5.1	66,981	94,129
Variable rate subordinate note	6/2035	7.3	10,785	10,785
Fixed rate subordinate note	6/2035	5.6	52,127	52,127
Unamortized premium/discount			(68)	(90)
2006-1 asset backed notes:				
Variable rate senior note	9/2035	5.7	53,953	102,252
Fixed rate senior note	9/2035	5.5	96,561	96,561
Fixed rate lockout senior note	9/2035	5.6	24,264	24,264
Unamortized premium/discount			(13)	(19)
2006-2 asset backed notes:				
Variable rate senior note	2/2036	5.6	92,126	136,386
Fixed rate senior note	2/2036	6.3	80,033	80,033
Fixed rate lockout senior note	2/2036	6.2	21,348	21,348
Unamortized premium/discount			(15)	(21)
2006-3 asset backed notes:				
Variable rate senior note	1/2037-9/2037	5.6	90,174	130,326
Fixed rate senior note	9/2037	5.9	67,050	67,050
Fixed rate lockout senior note	9/2037	5.9	18,000	18,000
Unamortized premium/discount			(8)	(11)
2007-1 asset backed notes:				
Variable rate senior note	8/2037	5.7	142,209	
Fixed rate senior note	8/2037	6.0	91,346	
Fixed rate lockout senior note	8/2037	5.9	22,000	
Unamortized premium/discount			(18)	
Total			$1,288,119	$1,173,012

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Note 8 Employee Retirement Plans

Components of net periodic cost of pension benefit:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
	(Dollars in thousands)			
Service cost	$ 1,072	$ 990	$ 3,217	$ 2,970
Interest cost	707	614	2,120	1,842
Expected return on plan assets	(627)	(563)	(1,880)	(1,689)
Amortization of transition obligation	3	2	8	6
Amortization of prior service cost	10	9	29	27
Amortization of actuarial loss	155	242	467	726
Net periodic benefit cost	$ 1,320	$ 1,294	$ 3,961	$ 3,882

As of September 30, 2007, we have not made any contributions to our pension plan in the current year and currently do not need to contribute to this plan in 2007 to maintain its funding status.

Note 9 Earnings Per Share

Earnings per share calculations are summarized as follows:

	Three Months ended September 30, 2007				
	Net Income (Loss)	Preferred Dividends	Basic Earnings Per Share	Effect of Stock Options	Diluted Earnings Per Share
	(Dollars in thousands, except per share amounts)				
Net income (loss) available to common shareholders:					
From Continuing Operations	$ (803)	$(326)	$ (1,129)	$ (279)	$ (1,408)
From Discontinued Operations	(17,227)		(17,227)		(17,227)
Total Net Loss for All Operations	$(18,030)	$(326)	(18,356)	(279)	(18,635)
Shares			29,191	1	29,192
Per-share from Continuing Operations			$ (0.04)	$ (0.01)	$ (0.05)
Per-share amount for All Operations			$ (0.63)	$ (0.01)	$ (0.64)

	Three Months ended September 30, 2006				
	Net	Preferred Dividends	Basic Earnings Per Share	Effect of	Diluted Earnings Per Share

	Income (Loss)			Stock Options	
	(Dollars in thousands, except per share amounts)				
Net income (loss) available to common shareholders:					
From Continuing Operations	$ 9,095	$	$ 9,095	$ (79)	$ 9,016
From Discontinued Operations	(13,302)		(13,302)		(13,302)
Total Net Income for All Operations	$ (4,207)	$	(4,207)	(79)	(4,286)
Shares			29,716	164	29,880
Per-share from Continuing Operations			$ 0.31	$ (0.01)	$ 0.30
Per-share amount for All Operations			$ (0.14)	$	$ (0.14)

	Nine Months ended September 30, 2007				
	Net Loss	Preferred Dividends	Basic Earnings Per Share	Effect of Stock Options	Diluted Earnings Per Share
	(Dollars in thousands, except per share amounts)				
Net loss available to common shareholders:					
From Continuing Operations	$ (1,425)	$(1,004)	$ (2,429)	$ (683)	$ (3,112)
From Discontinued Operations	(27,123)		(27,123)		(27,123)
Total Net Loss for All Operations	$(28,548)	$(1,004)	(29,552)	(683)	(30,235)
Shares			29,390	20	29,410
Per-share from Continuing Operations			$ (0.08)	$ (0.03)	$ (0.11)
Per-share amount for All Operations			$ (1.01)	$ (0.02)	$ (1.03)

	Nine Months ended September 30, 2006				
	Net Income (Loss)	Preferred Dividends	Basic Earnings Per Share	Effect of Stock Options	Diluted Earnings Per Share
	(Dollars in thousands, except per share amounts)				
Net income (loss) available to common shareholders:					
From Continuing Operations	$ 26,754	$	$ 26,754	$ (219)	$ 26,535
From Discontinued Operations	(29,948)		(29,948)		(29,948)
Total Net Income for All Operations	$ (3,194)	$	(3,194)	(219)	(3,413)
Shares			29,448	183	29,631
Per-share from Continuing Operations			$ 0.91	$ (0.01)	$ 0.90
Per-share amount for All Operations			$ (0.11)	$ (0.01)	$ (0.12)

At September 30, 2007 and 2006, 2,252,292 and 1,902,917 shares, respectively, related to stock options were not included in the dilutive earnings per share calculation because they had exercise prices above the stock price as of the

respective dates.

Note 10 Industry Segment Information

We have three principal business segments that provide a broad range of banking products and services, including commercial banking, commercial finance, and consumer mortgage products and services.

As described in Note 2, we have recently exited the conforming, conventional mortgage banking line of business. This segment is shown in the table below as Discontinued Operations. Our other segment primarily includes the parent company, unsold portions of businesses in which we no longer engage, and eliminations.

The accounting policies of each segment are the same as those described in Note 1 - Accounting Policies, Management Judgments and Accounting Estimates.

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Following is a summary of each segment s revenues, net income, and assets for the years indicated:

	Commercial Banking	Commercial Finance	Home Equity Lending	Other	Consolidated Continuing Operations	Discontinued Operations	Consolidated
	(Dollars in thousands)						
For the Three Months Ended September 30, 2007							
Net interest income	$27,818	$ 20,919	$ 5,747	$(17,831)	$ 36,653	$ (550)	$ 36,103
Intersegment interest	(929)	(10,521)	(4,875)	16,325			
Other revenues	4,099	3,480	2,150	(2,697)	7,032	(4,577)	2,455
Intersegment revenues			1,058	(1,058)			
Total net revenues	30,988	13,878	4,080	(5,261)	43,685	(5,127)	38,558
Other expense	22,650	7,199	16,968	(472)	46,345	23,640	69,985
Intersegment expenses	932	400	670	(2,002)			
Income (loss) before taxes	7,406	6,279	(13,558)	(2,787)	(2,660)	(28,767)	(31,427)
Income taxes	2,697	2,471	(5,420)	(1,605)	(1,857)	(11,540)	(13,397)
Net income (loss)	$ 4,709	$ 3,808	$ (8,138)	$ (1,182)	$ (803)	$(17,227)	$(18,030)
For the Three Months Ended September 30, 2006							
Net interest income	$29,652	$ 16,759	$ 26,935	$(17,184)	$ 56,162	$ 5,856	$ 62,018
Intersegment interest	618	(7,955)	(7,574)	14,911			
Other revenue	4,691	2,536	(820)	940	7,347	901	8,248
Total net revenues	34,961	11,340	18,541	(1,333)	63,509	6,757	70,266
Other expense	22,418	5,783	18,198	4,465	50,864	28,943	79,807
Intersegment expenses	691	286	812	(1,789)			
Income (loss) before taxes	11,852	5,271	(469)	(4,009)	12,645	(22,186)	(9,541)
Income taxes	3,594	1,997	(177)	(1,864)	3,550	(8,884)	(5,334)
Net income (loss)	$ 8,258	$ 3,274	$ (292)	$ (2,145)	$ 9,095	$(13,302)	$ (4,207)

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	Commercial Banking	Commercial Finance	Home Equity Lending	Other	Consolidated Continuing Operations	Discontinued Operations	Consolidated
	(Dollars in thousands)						
For the Nine Months Ended September 30, 2007							
Net interest income	$ 82,010	$ 57,695	$ 37,448	$ (51,191)	$ 125,962	$ (1,766)	$ 124,196
Intersegment interest	(1,084)	(28,898)	(18,228)	48,210			
Other revenue	12,234	9,218	(851)	(4,802)	15,799	(12,037)	3,762
Intersegment revenues			2,024	(2,024)			
Total net revenues	93,160	38,015	20,393	(9,807)	141,761	(13,803)	127,958
Other expense	68,097	21,458	52,121	4,017	145,693	31,570	177,263
Intersegment expenses	2,700	1,209	1,966	(5,875)			
Income (loss) before taxes	22,363	15,348	(33,694)	(7,949)	(3,932)	(45,373)	(49,305)
Income taxes	8,149	6,013	(13,456)	(3,213)	(2,507)	(18,250)	(20,757)
Net income (loss)	$ 14,214	$ 9,335	$ (20,238)	$ (4,736)	$ (1,425)	$ (27,123)	$ (28,548)
Assets at September 30, 2007	$ 3,131,124	$ 1,251,874	$ 1,561,817	$ 217,033			$ 6,161,848
For the Nine Months Ended September 30, 2006							
Net interest income	$ 82,916	$ 46,541	$ 83,374	$ (47,239)	$ 165,592	$ 20,236	$ 185,828
Intersegment interest	5,814	(20,886)	(27,678)	42,750			
Other revenue	13,553	6,684	10,149	3	30,389	16,035	46,424
Total net revenues	102,283	32,339	65,845	(4,486)	195,981	36,271	232,252
Other expense	64,104	16,877	62,683	11,308	154,972	86,183	241,155
Intersegment expenses	2,062	840	2,519	(5,421)			
Income (loss) before taxes	36,117	14,622	643	(10,373)	41,009	(49,912)	(8,903)
Income taxes	13,245	5,525	283	(4,798)	14,255	(19,964)	(5,709)
Net income (loss)	$ 22,872	$ 9,097	$ 360	$ (5,575)	$ 26,754	$ (29,948)	$ (3,194)
Assets at September 30, 2006	$ 3,058,334	$ 1,012,502	$ 1,536,519	$ 389,140			$ 5,996,495

Note 11 Commitments and Contingencies

Culpepper v. Inland Mortgage Corporation

On July 2, 2007, the Court of Appeals for the 11th Circuit affirmed the decision of the United States District Court for the Northern District of Alabama granting summary judgment in favor of our indirect subsidiary, Irwin Mortgage Corporation (formerly Inland Mortgage Corporation), and decertifying the plaintiffs class. On July 13, 2007, plaintiffs filed a petition for a rehearing en banc. This lawsuit was originally filed in April 1996 alleging that Irwin Mortgage s payment of broker fees to mortgage brokers violated the federal Real Estate Settlement Procedures Act. In its July 2, 2007, decision, and based on the test set forth in the Department of Housing and Urban Development s 2001 policy statement on lender payments to mortgage brokers, the court of appeals affirmed summary judgment for Irwin Mortgage because the plaintiffs failed to show that the total compensation Irwin Mortgage paid to the mortgage brokers was unreasonable in light of the services provided. The court of appeals also held that the district court did not abuse its discretion in decertifying the plaintiffs class because the individualized assessment required in this type of action made class certification inappropriate. We await a decision of the court of appeals on the plaintiffs petition. We have not established any reserves for this case.

Silke v. Irwin Mortgage Corporation

In April 2003, our indirect subsidiary, Irwin Mortgage Corporation, was named as a defendant in a class action lawsuit filed in the Marion County, Indiana, Superior Court. The complaint alleged that Irwin Mortgage charged a document preparation fee in violation of Indiana law for services performed by clerical personnel in completing legal documents related to mortgage loans. On June 18, 2004, the court certified a plaintiff class and held oral argument on cross-motions for summary judgment on April 30, 2007. On May 2, 2007, the Indiana Supreme Court issued an opinion in another case, *Charter One Mortgage Corporation v. Condra,* which held that the preparation of mortgage documents by non-attorneys does not necessarily constitute the practice of law and that a lender s charging a fee for the preparation does not convert it into the unauthorized practice of law. Citing the *Charter One* decision, on August

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27, 2007, the *Silke* trial court ruled in favor of Irwin Mortgage on its Motion for Summary Judgment against plaintiff class members, thus concluding this litigation.

Cohens v. Inland Mortgage Corporation

In October 2003, our indirect subsidiary, Irwin Mortgage Corporation, was named as a defendant, along with others, in an action filed in the Supreme Court of New York, County of Kings. The plaintiffs, a mother and two children, allege they were injured from lead contamination while living in premises allegedly owned by the defendants. The suit seeks approximately $41 million in damages and alleges negligence, breach of implied warranty of habitability and fitness for intended use, loss of services and the cost of medical treatment. On September 15, 2005, Irwin Mortgage filed an answer and cross-claims seeking dismissal of the complaint. On October 13, 2006, Irwin Mortgage filed a motion for summary judgment. In May 2007, the court disposed of this case due to lack of prosecution by the plaintiffs but restored the action based on a motion by plaintiffs on June 28, 2007. We filed an affirmation in support of our motion for summary judgment on July 10, 2007. We have not established any reserves for this case.

Litigation in Connection with Loans Purchased from Community Bank of Northern Virginia

Our subsidiary, Irwin Union Bank and Trust Company, is a defendant in several actions in connection with loans Irwin Union Bank purchased from Community Bank of Northern Virginia (Community).

Hobson v. Irwin Union Bank and Trust Company was filed on July 30, 2004 in the United States District Court for the Northern District of Alabama. As amended on August 30, 2004, the *Hobson* complaint, seeks certification of both a plaintiffs   and a defendants   class, the plaintiffs   class to consist of all persons who obtained loans from Community and whose loans were purchased by Irwin Union Bank. *Hobson* alleges that defendants violated the Truth-in-Lending Act (TILA), the Home Ownership and Equity Protection Act (HOEPA), the Real Estate Settlement Procedures Act (RESPA) and the Racketeer Influenced and Corrupt Organizations Act (RICO). On October 12, 2004, Irwin filed a motion to dismiss the *Hobson* claims as untimely filed and substantively defective.

Kossler v. Community Bank of Northern Virginia was originally filed in July 2002 in the United States District Court for the Western District of Pennsylvania. Irwin Union Bank and Trust was added as a defendant in December 2004. The *Kossler* complaint seeks certification of a plaintiffs   class and seeks to void the mortgage loans as illegal contracts. Plaintiffs also seek recovery against Irwin for alleged RESPA violations and for conversion. On September 9, 2005, the *Kossler* plaintiffs filed a Third Amended Class Action Complaint. On October 21, 2005, Irwin filed a renewed motion seeking to dismiss the *Kossler* action.

The plaintiffs in *Hobson* and *Kossler* claim that Community was allegedly engaged in a lending arrangement involving the use of its charter by certain third parties who charged high fees that were not representative of the services rendered and not properly disclosed as to the amount or recipient of the fees. The loans in question are allegedly high cost/high interest loans under Section 32 of HOEPA. Plaintiffs also allege illegal kickbacks and fee splitting. In *Hobson*, the plaintiffs allege that Irwin was aware of Community   s alleged arrangement when Irwin purchased the loans and that Irwin participated in a RICO enterprise and conspiracy related to the loans. Because Irwin bought the loans from Community, the *Hobson* plaintiffs are alleging that Irwin has assignee liability under HOEPA.

If the *Hobson* and *Kossler* plaintiffs are successful in establishing a class and prevailing at trial, possible RESPA remedies could include treble damages for each service for which there was an unearned fee, kickback or overvalued service. Other possible damages in *Hobson* could include TILA remedies, such as rescission, actual damages, statutory damages not to exceed the lesser of $500,000 or 1% of the net worth of the creditor, and attorneys   fees and costs; possible HOEPA remedies could include the refunding of all closing costs, finance charges and fees paid by the borrower; RICO remedies could include treble plaintiffs   actually proved damages. In addition, the *Hobson* plaintiffs are seeking unspecified punitive damages. Under TILA, HOEPA, RESPA and RICO, statutory remedies include recovery of attorneys   fees and costs. Other possible damages in *Kossler* could include the refunding of all origination fees paid by the plaintiffs.

Irwin Union Bank and Trust Company is also a defendant, along with Community, in two individual actions *(Chatfield v. Irwin Union Bank and Trust Company, et al.* and *Ransom v. Irwin Union Bank and Trust Company, et al.)* filed on September 9, 2004 in the Circuit Court of Frederick County, Maryland, involving mortgage loans Irwin

Union Bank purchased from Community. On July 16, 2004, both of these lawsuits were removed to the United States District Court for the District of Maryland. The complaints allege that the plaintiffs did not receive disclosures required under HOEPA and TILA. The lawsuits also allege violations of Maryland law

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because the plaintiffs were allegedly charged or contracted for a prepayment penalty fee. Irwin believes the plaintiffs received the required disclosures and that Community, a Virginia-chartered bank, was permitted to charge prepayment fees to Maryland borrowers.

Under the loan purchase agreements between Irwin and Community, Irwin has the right to demand repurchase of the mortgage loans and to seek indemnification from Community for the claims in these lawsuits. On September 17, 2004, Irwin made a demand for indemnification and a defense to *Hobson, Chatfield* and *Ransom.* Community denied this request as premature.

In response to a motion by Irwin, the Judicial Panel On Multidistrict Litigation consolidated *Hobson, Chatfield* and *Ransom* with *Kossler* in the Western District of Pennsylvania for all pretrial proceedings. The Pennsylvania District Court had been handling another case seeking class action status, *Kessler v. RFC, et al*., also involving Community and with facts similar to those alleged in the Irwin consolidated cases. The *Kessler* case had been settled, but the settlement was appealed and set aside on procedural grounds. Subsequently, the parties in *Kessler* filed a motion for approval of a modified settlement, which would provide additional relief to the settlement class. Irwin is not a party to the *Kessler* action, but the resolution of issues in *Kessler* may have an impact on the Irwin cases. The Pennsylvania District Court has effectively stayed action on the Irwin cases until issues in the *Kessler* case are resolved. On July 5, 2007, the *Amicus Curiae* (Friend of the Court) appointed by the Pennsylvania District Court to evaluate the fairness of the modified *Kessler* settlement issued his Advisory Opinion, which found the proposed modified *Kessler* settlement to be fair and reasonable. We have established a reserve for the Community litigation based upon SFAS 5 guidance and the advice of legal counsel.

Putkowski v. Irwin Home Equity Corporation and Irwin Union Bank and Trust Company

On August 12, 2005, our indirect subsidiary, Irwin Home Equity Corporation, and our direct subsidiary, Irwin Union Bank and Trust Company (collectively, Irwin), were named as defendants in litigation seeking class action status in the United States District Court for the Northern District of California for alleged violations of the Fair Credit Reporting Act. In response to Irwin s motion to dismiss filed on October 18, 2005, the court dismissed the plaintiffs complaint with prejudice on March 23, 2006. Plaintiffs filed an appeal in the U.S. Court of Appeals for the 9th Circuit on April 13, 2006. We have not established any reserves for this case.

We and our subsidiaries are from time to time engaged in various matters of litigation, including the matters described above, other assertions of improper or fraudulent loan practices or lending violations, and other matters, and we have a number of unresolved claims pending. In addition, as part of the ordinary course of business, we and our subsidiaries are parties to litigation involving claims to the ownership of funds in particular accounts, the collection of delinquent accounts, challenges to security interests in collateral, and foreclosure interests, that is incidental to our regular business activities. While the ultimate liability with respect to these other litigation matters and claims cannot be determined at this time, we believe that damages, if any, and other amounts relating to pending matters are not likely to be material to our consolidated financial position or results of operations, except as described above. Reserves are established for these various matters of litigation, when appropriate under SFAS 5, based in part upon the advice of legal counsel.

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

About Forward-looking Statements

You should read the following discussion in conjunction with our consolidated financial statements, footnotes, and tables. This discussion and other sections of this report contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. We intend such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. We are including this statement for purposes of invoking these safe harbor provisions.

Forward-looking statements are based on management s expectations, estimates, projections, and assumptions. These statements involve inherent risks and uncertainties that are difficult to predict and are not guarantees of future performance. In addition, our past results of operations do not necessarily indicate our future results. Words that convey our beliefs, views, expectations, assumptions, estimates, forecasts, outlook and projections or similar language, or that indicate events we believe could, would, should, may or will occur (or might not occur) or are likely

(or unlikely) to occur, and similar expressions, are intended to identify forward-looking statements. These may include, among other things, statements and assumptions about:

- our projected revenues, earnings or earnings per share, as well as management s short-term and long-term performance goals;

projected trends or potential changes in asset quality (particularly with regard to loans or other exposures including loan repurchase risk, in sectors in which we deal in real estate or residential mortgage lending), loan delinquencies, charge-offs, reserves, asset valuations, capital ratios or financial performance measures;

our plans and strategies, including the expected results or costs and impact of implementing or changing such plans and strategies;

potential litigation developments and the anticipated impact of potential outcomes of pending legal matters;

predictions about conditions in the mortgage markets or mortgage industry;

the anticipated effects on results of operations or financial condition from recent developments or events; and

any other projections or expressions that are not historical facts.

We qualify any forward-looking statements entirely by these cautionary factors.

Actual future results may differ materially from what is projected due to a variety of factors, including, but not limited to:

potential deterioration of general economic conditions, particularly in sectors relating to real estate and/or mortgage lending or small business-based manufacturing;

potential changes in direction, volatility and relative movement (basis risk) of interest rates, which may affect consumer demand for our products and the management and success of our interest rate risk management strategies;

competition from other financial service providers for experienced managers as well as for customers;

staffing fluctuations in response to product demand or the implementation of corporate strategies that affect our work force;

the relative profitability of our lending operations;

the valuation and management of our portfolios, including the use of external and internal modeling assumptions we embed in the valuation of those portfolios and short-term swings in the valuation of such portfolios;

borrowers refinancing opportunities, which may affect the prepayment assumptions used in our valuation estimates and which may affect loan demand;

unanticipated deterioration in the credit quality or collectibility of our loan and lease assets, including deterioration resulting from the effects of natural disasters;

difficulties in accurately estimating the future repurchase risk of residential mortgage loans due to alleged violations of representations and warranties we made when selling the loans to the secondary market;

unanticipated deterioration or changes in estimates of the carrying value of our other assets, including securities;

difficulties in delivering products to the secondary market as planned;

difficulties in expanding our businesses and obtaining funding sources as needed;

changes in the value of our lines of business, subsidiaries, or companies in which we invest;

changes in variable compensation plans related to the performance and valuation of lines of business where we tie compensation systems to line-of-business performance;

unanticipated outcomes in litigation;

legislative or regulatory changes, including changes in laws, rules or regulations that affect tax, consumer or commercial lending, corporate governance and disclosure requirements, and other laws, rules or regulations affecting the rights and responsibilities of our Corporation, bank or thrift;

regulatory actions that impact our Corporation, bank or thrift, including the memorandum of understanding entered into as of March 1, 2007 between Irwin Union Bank and Trust and the Federal Reserve Bank of Chicago;

changes in the interpretation of regulatory capital or other rules;

the availability of resources to address changes in laws, rules or regulations or to respond to regulatory actions;

changes in applicable accounting policies or principles or their application to our business or final audit adjustments, including additional guidance and interpretation on accounting issues and details of the implementation of new accounting methods;

the final disposition of our remaining assets and obligations of our discontinued mortgage banking segment; or

governmental changes in monetary or fiscal policies.

We undertake no obligation to update publicly any of these statements in light of future events, except as required in subsequent reports we file with the Securities and Exchange Commission (SEC).

Strategy

Our strategy is to create competitive advantage within the banking industry by serving niche markets of small businesses with lending, leasing, deposit and advisory services and consumers primarily with specialized mortgage products. Our strategic objective is to create value through well-controlled, profitable growth by: i) focusing on meeting customer needs rather than simply offering banking products or services, ii) being cost-efficient in our delivery, and iii) having strong risk management systems. We believe we must continually balance these three factors in order to deliver long-term value to all of our stakeholders.

We have developed several tactics to meet these goals:

1. *Identify market niches.*. Based on our assessment of long-term market, customer and competitive trends and opportunities, we focus on product or market niches in banking for small businesses and consumers where our understanding of customer needs and ability to meet them creates added value that permits us not to have to compete primarily on price. We do not believe it is necessary to be the largest or leading market share company in any of our product lines to earn an adequate risk-adjusted return, but we do believe it is important that we are viewed as a preferred provider in niche segments of those product offerings. We believe the most attractive opportunities at present are in providing small businesses with lending, leasing, deposit and advisory services and consumers with specialized mortgage products.

2. *Attract, develop and retain exceptional management with niche expertise.* We participate in lines of business only when we have attracted senior managers who have proven track records in the niche for which they are responsible. Our structure allows managers to focus their efforts on understanding their customers, meeting the needs of the markets they serve cost effectively, and identifying and controlling the risks inherent in their activities. This structure also promotes accountability among managers of each segment. We attempt to create a mix of short-term and long-term rewards that provide these managers with the incentive to achieve well-controlled, profitable growth over the long term.

3. *Diversify capital and earnings risk.* We diversify our revenues, credit risk, and application of capital across complementary lines of business and across different regions as a key part of our risk management. For example, the customers of our commercial

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bank have different growth and risk profiles in the Midwest and West. These markets perform differently due to differences in local economies, affecting both demand and credit quality of our products. Our home equity segment lends to consumers on a national basis, building a diversified portfolio where demand and credit quality fluctuate depending, in part, on local market conditions. Our customers credit needs are cyclical, but when combined in an appropriate mix, we believe they provide sources of diversification and opportunities for growth in a variety of economic conditions.

4. *Focus on organic growth.* We primarily focus on growth through organic expansion of existing lines of business as we believe this approach often provides a better risk/return profile. Over the past ten years, we have made only a few acquisitions. Those have typically not been in competitive bidding situations.

5. *Identify opportunities for coordination and efficiencies across the Bank.* We have recently increased our attention to the identification of areas in which we can better coordinate and consolidate non-customer facing operations within our segments. Our objective is to improve risk management and operating efficiency without diminishing our ability to provide a high level of service to our customers. Our efforts to date have focused on the centralization of certain risk management functions, as well as improvements in information technologies and procurement through shared services.

6. *Create and maintain risk management systems appropriate to our size, scale and scope.* These systems are an integral part of a well-managed banking organization and are as important to our future success as hiring good people and offering products and services in attractive niches. We are engaged in a multiyear process of enhancing our management depth and systems for assuring that we operate our businesses within the risk appetite established by our board of directors. The system we are creating provides centralized guidance and support from staff with demonstrated risk management expertise, who provide an independent perspective assessing and assisting the risk management processes and systems that are an integral part of each of our managers responsibilities.

We believe long-term growth and profitability will result from our endeavors to serve attractive niches within commercial and consumer banking, our experienced management, our diverse products and geographic markets, and our focus on risk management systems.

Critical Accounting Policies

Accounting estimates are an integral part of our financial statements and are based upon our current judgments. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ from our current judgments or that our use of different assumptions could result in materially different estimates. Our Annual Report on Form 10-K for the year ended 2006 provides a description of the critical accounting policies we apply to material financial statement items, all of which require the use of accounting estimates and/or judgment.

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Consolidated Overview

As discussed below, the financial statements, footnotes, schedules and discussion within this report have been reformatted to conform to the presentation required for discontinued operations pursuant to our sale of our mortgage banking line of business.

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2007	2006	2007	2006
Net income (loss) from continuing operations (in thousands)	$ (803)	$ 9,095	$ (1,425)	$26,754
Net loss including discontinued operations (in thousands)	(18,030)	(4,207)	(28,548)	(3,194)
Basic earnings per share from continuing operations	(0.04)	0.31	(0.08)	0.91
Basic earnings per share including discontinued operations	(0.63)	(0.14)	(1.01)	(0.11)
Diluted earnings per share from continuing operations	(0.05)	0.30	(0.11)	0.90
Diluted earnings per share including discontinued operations	(0.64)	(0.14)	(1.03)	(0.12)
Return on average equity from continuing operations	(0.6)%	6.7%	(0.4)%	6.7%
Return on average assets from continuing operations	(0.1)%	0.6%	0.0%	0.5%
Net interest margin			4.53%	4.67%

Consolidated Income Statement Analysis

Net Income from Continuing Operations

We recorded a net loss from continuing operations of $0.8 million for the three months ended September 30, 2007, down from net income from continuing operations of $9.1 million for the three months ended September 30, 2006. Net loss per share (diluted) was $0.05 for the quarter ended September 30, 2007, down from $0.30 per share for the second quarter of 2006. For the year to date, we recorded a net loss from continuing operations of $1.4 million or $0.11 per diluted share compared to net income of $26.8 million or $0.90 per share in 2006.

Our consolidated performance in the first nine months of 2007 was negatively affected by a significant deterioration of the mortgage markets. This has lead to a material loss in the home equity and discontinued mortgage operations segments as a result of increasing provision for loan losses. During the third quarter of 2007, we provided $28 million in loan loss provision. This provision is based on significant revisions in our expectations of future losses that have not yet been incurred. We currently believe these reserves adequately reflect our risk of loss in the current and expected environment.

Net Interest Income from Continuing Operations

Net interest income from continuing operations for the nine months ended September 30, 2007 totaled $197 million, up 3% from net interest income of $191 million in the same period in 2006. Net interest margin for the nine months ended September 30, 2007 was 4.53%, down slightly compared to 4.67% for the same period in 2006.

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The following table shows our daily average consolidated balance sheet, interest rates and yield at the dates indicated:

	For the Nine Months Ended September 30,					
	2007			2006		
	Average Balance	Interest	Annualized Yield/ Rate	Average Balance	Interest	Annualized Yield/ Rate
	(Dollars in thousands)					
Assets						
Interest-earning assets:						
Interest-bearing deposits with financial institutions	$ 52,648	$ 2,093	5.32%	$ 73,841	$ 2,089	3.78%
Federal funds sold	19,667	602	4.09%	4,600	137	3.98%
Residual interests	10,196	817	10.71%	14,408	1,409	13.07%
Investment securities	137,989	5,664	5.49%	112,582	4,040	4.80%
Loans held for sale	124,528	6,677	7.17%	1,059,537	67,610	8.53%
Loans and leases, net of unearned income [(1)]	5,426,759	371,502	9.15%	4,776,255	318,088	8.90%
Total interest earning assets	5,771,787	$ 387,355	8.97%	6,041,223	$ 393,373	8.71%
Noninterest-earning assets:						
Cash and due from banks	72,880			109,991		
Premises and equipment, net	39,092			33,293		
Other assets	296,246			518,659		
Less allowance for loan and lease losses	(87,384)			(65,865)		
Total assets	$ 6,092,621			$ 6,637,301		
Liabilities and Shareholders Equity						
Interest-bearing liabilities:						
Money market checking	$ 283,746	$ 4,890	2.30%	$ 376,826	$ 6,772	2.40%
Money market savings	1,160,416	38,954	4.49%	1,174,114	35,936	4.09%
Regular savings	124,113	2,064	2.22%	133,501	1,799	1.80%
Time deposits	1,497,477	57,270	5.11%	1,585,335	54,115	4.56%
Short-term borrowings	621,873	24,329	5.23%	619,367	29,564	6.38%
Collateralized debt	1,223,586	51,491	5.63%	941,966	37,013	5.25%
Other long-term debt	233,930	13,005	7.43%	250,866	17,164	9.15%
Total interest-bearing liabilities	$ 5,145,141	$ 192,003	4.99%	$ 5,081,975	$ 182,363	4.80%
Noninterest-bearing liabilities:						

Demand deposits	334,639			767,614		
Other liabilities	98,946			256,579		
Shareholders equity	513,895			531,133		
Total liabilities and shareholders equity	$ 6,092,621			$ 6,637,301		
Net interest income		$ 195,352			$ 211,010	
Net interest income to average interest earning assets			4.53%			4.67%
Less: Net interest income from discontinued operations		(1,765)			20,264	
Net interest income from continuing operations		$ 197,117			$ 190,746	

(1) For purposes of these computations, nonaccrual loans are included in daily average loan amounts outstanding.

Provision for Loan and Lease Losses from Continuing Operations

The consolidated provision for loan and lease losses for the three months ended September 30, 2007 was $28 million, compared to $9 million for the same period in 2006. Year to date, the provision for 2007 was $71 million, compared to $25 million for the same period in 2006. More information on this subject is contained in the section on credit risk.

Noninterest Income from Continuing Operations

Noninterest income during the three months ended September 30, 2007 totaled $7 million, unchanged from the same period of 2006. Noninterest income of $16 million was recorded for the nine months ended September 30, 2007 and $30 million for the same period in 2006. The decrease in year-to-date 2007 versus 2006 related primarily to the home equity line of business where there were higher valuation adjustments on loans held for sale, lower servicing revenues, and lower derivative gains. Details related to these fluctuations are discussed later in the home equity lending section of this document.

Noninterest Expense from Continuing Operations

Noninterest expenses for the three and nine months ended September 30, 2007 totaled $46 million and $146 million, respectively, compared to $51 million and $155 million for the same periods in 2006. The decrease in consolidated noninterest expense in 2007 is primarily due to decreases in the home equity line of business variable compensation costs. Details related to these fluctuations are discussed later in the home equity lending section of this document.

Income Tax Provision from Continuing Operations

Income tax benefit for the three months and nine months ended September 30, 2007 totaled $1.9 million and $2.5 million, compared to tax provision of $3.6 million and $14.3 million during the same periods in 2006. The effective tax rate in 2007 is skewed by permanent favorable tax adjustments during a period of near break-even results. The third quarter 2007 results include a $0.4 million reversal of tax reserves.

Consolidated Balance Sheet Analysis

Total assets at September 30, 2007 were $6.2 billion, down 1% from December 31, 2006. Average assets for the first nine months of 2007 were $6.1 billion, down 7% from the average assets for the year ended December 31, 2006. The decline in the consolidated average balance sheet reflects the sale of the majority of the mortgage banking line of business assets, offset only in part by growth in our commercial portfolios. At September 30, 2007, $8 million of assets from our mortgage banking segment were classified as assets held for sale on our balance sheet pending the planned sale of these assets.

Investment Securities

The following table shows the composition of our investment securities at the dates indicated:

	September 30, 2007	December 31, 2006
	(Dollars in thousands)	
U.S. Treasury and government obligations	$ 13,549	$ 13,730
Obligations of states and political subdivisions	3,436	3,545
Mortgage-backed securities	47,398	45,187
Other	77,407	65,968
Total	$ 141,790	$ 128,430

Loans Held For Sale

Loans held for sale totaled $3 million at September 30, 2007, a decrease from a balance of $238 million at December 31, 2006. The reduction occurred primarily at our home equity line of business where we reclassified $167 million of mortgage loans held for sale to held for investment during the first quarter reflecting our decision not to sell into weak secondary market conditions. New production of home equity product is now being classified as held for investment. Details related to this reclassification are discussed later in the home equity lending section of this document.

Loans and Leases

Our commercial loans and leases are originated throughout the United States and Canada. At September 30, 2007, 93% of our loan and lease portfolio was associated with our U.S. operations. We also extend credit to consumers throughout the United States through mortgages, installment loans and revolving credit arrangements. Loans by major category for the periods presented were as follows:

	September 30, 2007	**December 31, 2006**
	(Dollars in thousands)	
Commercial, financial and agricultural	$2,290,394	$2,249,988
Residential real estate-construction	381,462	377,601
Residential real estate-mortgage	1,737,437	1,522,616
Consumer	33,085	31,581
Commercial financing		
Franchise financing	838,317	699,969
Domestic leasing	307,958	296,056
Canadian leasing	459,798	358,783
Unearned income		
Franchise financing	(270,814)	(211,480)
Domestic leasing	(43,693)	(42,782)
Canadian leasing	(57,254)	(44,139)
Total	$5,676,690	$5,238,193

Allowance for Loans and Lease Losses

Deposits

Year-to-date deposits for 2007 averaged $3.4 billion compared to deposits for the year 2006 that averaged $4.0 billion. Year-to-date demand deposits for 2007 averaged $0.3 billion, a 56% decrease over the average balance for the year 2006. In 2006, demand deposits totaling $0.4 billion in 2006 related to deposits at Irwin Union Bank and Trust Company (IUBT) which were associated with escrow accounts held on loans in the servicing portfolio at the discontinued mortgage banking line of business. These escrow accounts

were transferred out of IUBT in early 2007 in connection with the transfer of mortgage servicing rights at the mortgage banking line of business.

Irwin Union Bank and Trust utilizes institutional broker-sourced deposits as funding to supplement deposits solicited through branches and other wholesale funding sources. At September 30, 2007, institutional broker-sourced deposits totaled $0.6 billion, compared to $0.5 billion at December 31, 2006.

Short-Term Borrowings

Year-to-date short-term borrowings for 2007 averaged $622 million compared to an average of $544 million for the year 2006. Short-term borrowings totaled $539 million at September 30, 2007, compared to $602 million at December 31, 2006. The increase in average short-term borrowings during 2007 compared to 2006 reflects declining deposit balances during 2007.

Federal Home Loan Bank borrowings averaged $489 million for the nine months ended September 30, 2007, with an average rate of 5.1%. At September 30, 2007 the balance was $465 million at an interest rate of 5.1%. The maximum outstanding during any month end during the nine months of 2007 was $565 million. Federal Home Loan Bank borrowings averaged $322 million for the year ended December 31, 2006, with an average rate of 4.9%. The balance at December 31, 2006 was $372 million at an interest rate of 5.0%. The maximum outstanding during any month end during 2006 was $609 million.

Collateralized and Other Long-Term Debt

Collateralized debt totaled $1.3 billion at September 30, 2007, compared to $1.2 billion at December 31, 2006. The bulk of these borrowings resulted from securitization of portfolio loans at the home equity lending line of business that results in loans remaining as assets and debt being recorded on the balance sheet. The securitization debt represents match-term funding for these loans.

Other long-term debt totaled $234 million at September 30, 2007 and December 31, 2006. We have obligations represented by subordinated debentures totaling $204 million with our wholly-owned trusts that were created for the purpose of issuing these securities. The subordinated debentures were the sole assets of the trusts at September 30, 2007. In accordance with FASB Interpretation No. 46 (FIN 46), Consolidation of Variable Interest Entities (revised December 2004), we deconsolidate the wholly-owned trusts that issued the trust preferred securities. As a result, these securities are no longer consolidated on our balance sheet. Instead, the subordinated debentures held by the trusts are disclosed on the balance sheet as other long-term debt.

Capital

Year-to-date shareholders equity averaged $514 million during 2007, down 2% compared to the average for the year 2006. Shareholders equity balance of $489 million at September 30, 2007 represented $16.25 per common share, compared to $17.30 per common share at December 31, 2006. We paid $3.5 million and $10.5 million in dividends for the three and nine months ended September 30, 2007, respectively, reflecting an increase of $0.01 and $0.03 per share, respectively, compared to a year ago. We also paid $0.3 million and $1.0 million for the three and nine months ended September 30, 2007, respectively, in preferred dividends on our noncumulative perpetual preferred stock.

The following table sets forth our capital and regulatory capital ratios at the dates indicated:

	September 30, 2007	December 31, 2006
	(Dollars in thousands)	
Tier 1 capital	$ 657,218	$ 712,403
Tier 2 capital	141,246	125,351
Total risk-based capital	$ 798,464	$ 837,754
Risk-weighted assets	$ 6,174,811	$ 6,258,927
Risk-based ratios:		
Tier 1 capital	10.6%	11.4%
Total capital	12.9	13.4
Tier 1 leverage ratio	10.8	11.5
Ending shareholders equity to assets	7.9	8.5
Average shareholders equity to assets	8.4	8.1

At September 30, 2007, our total risk-adjusted capital ratio was 12.9% exceeding our Policy internal minimum of 11.0% (we have a higher Policy minimum, 12.0%, at our principal subsidiary, Irwin Union Bank and Trust). At December 31, 2006, our total risk-adjusted capital ratio was 13.4%. Our ending equity to assets ratio at September 30, 2007 was 7.9% compared to 8.5% at December 31, 2006. Our Tier 1 capital totaled $657 million as of September 30, 2007, or 10.6% of risk-weighted assets.

Retained earnings increased by $1.7 million during 2007 as a result of our adoption of FAS 156 related to accounting for mortgage servicing rights. In accordance with this pronouncement, we recorded as an increase to retained earnings a $1.7 million one time (tax-affected) cumulative adjustment on January 1, 2007.

Cash Flow Analysis

Year-to-date, our cash and cash equivalents decreased $60 million during 2007, compared to a decrease of $24 million during the same period in 2006. Cash flows from operating activities provided $0.2 billion in cash and cash equivalents for the nine months ended September 30, 2007 compared to the same period in 2006 when our operations provided $1.1 billion in cash and cash equivalents. Year-to-date in 2007, accounts receivable decreased $163 million which increased cash provided by operating activities during that period.

Earnings Outlook

Our strategy is to seek opportunities for well-controlled, profitable growth by serving niche markets while attempting to mitigate the impact of changes in interest rates and economic conditions on our credit retained portfolios. Although at present we are not meeting our targets, we believe this strategy can, over time, provide above market growth rates in earnings per share and return on equity. Prior to 2005, a meaningful amount of our earnings, in many years, came from our conforming conventional first mortgage segment. We decided to exit this line of business in 2006 due to changes in the environment and competitive conditions. Opportunities in our remaining three segments continue to grow across the U.S. and, in our commercial finance segment, also in Canada. We believe this growth will contribute in a meaningful way to the Corporation s future success.

Our consolidated performance in 2007 has been negatively affected by a significant deterioration of the mortgage markets. This has lead to a material loss in the home equity and discontinued mortgage operations segments as a result of increasing provisions for loan losses. During the third quarter of 2007, we provided $27 million in loan loss provision and $17 million in additional reserves for potential loan repurchases. These provisions represent valuation adjustments due to current market conditions and our expectations of future losses that have not yet been incurred.

Home equity s performance continues to be challenged by the adverse conditions in the industry. The segment provides credit and geographic diversification for commercial portfolios. If we are able to return it to acceptable financial performance, we believe in the long run it can generate excess capital to grow the commercial segments.

Achieving this strategic intent is proving quite difficult in the short term as we are in the midst of making significant structural changes in this segment in the face of an external market environment undergoing extensive

disruption resulting from increased losses in the mortgage industry. If our initiatives are successful and the external market environment normalizes, we believe that this segment can achieve both our financial goals of double digit earnings growth and a return in excess of the cost of capital.

We have taken substantial steps to reduce our home equity operating expenses. Since July 1, 2007 we have reduced the number of employees by approximately 130, as compared to staff of approximately 460 as of June 30, 2007. Management is actively reassessing the operating expense of the segment. During the third quarter of 2007, $1.1 million of severance costs were incurred. Additional steps will be taken in the fourth quarter, including the reduction of production and related staffing. This includes the consolidation and reduction of the east coast mortgage operations center in Charlotte and certain additional positions in an effort to align costs with current market opportunities. The Corporation believes the bulk of these severance, lease termination, and fixed-asset disposal costs will be recognized in the fourth quarter, although certain actions are likely to carry over into early 2008.

In addition to the steps we are taking in the home equity segment, we are in the midst of taking action elsewhere in the Corporation where our results have been disappointing, to align staffing with the current environment. We have not completed our plans, but in combination with expected actions at the home equity segment, we expect future restructuring charges in the range of $10 to $15 million pre-tax, with the expectation that the bulk of this will be reflected in the fourth quarter

Our methodology for developing reserves for loan repurchase risk is described further in the section of this report on Discontinued Operations. While we currently believe these reserves adequately reflect our risk of loss in the current and expected environment, we are using these models to project losses during an environment with little precedent. As an example, from January through July of 2007, we had received an average of 17 repurchase requests per month, with modest month-to-month volatility. During August, the number of requests spiked to 33, only to slow to 12 in September (and at the time of writing of this filing, less than 15 in October). We will update the reserve models as more data is available.

In summary, the current environment is one in which accurate earnings forecasts are difficult to make. We believe our two commercial segments will continue to deliver profitable results over the near-term, with good quarterly improvement. The external environment is making it much more difficult, however, to assess near-term conditions in the mortgage markets. We believe we have adequately addressed loan loss and repurchase risk in our home equity segment and Discontinued Operation through the significant reserves we have taken in recent months. Assuming external conditions do not deteriorate further and prior to the anticipated restructuring charges noted above, we expect a return to modest Continuing Operations profitability during the fourth quarter and good earnings in 2008.

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Earnings by Line of Business

Irwin Financial Corporation is composed of three principal lines of business:

- Commercial Banking
- Commercial Finance
- Home Equity Lending

The following table summarizes our net income (loss) by line of business for the periods indicated:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
	(Dollars in thousands)			
Net income (loss):				
Commercial Banking	$ 4,709	$ 8,258	$ 14,214	$ 22,872
Commercial Finance	3,808	3,274	9,335	9,097
Home Equity Lending	(8,138)	(292)	(20,238)	360
Other (including consolidating entries)	(1,182)	(2,145)	(4,736)	(5,575)
Net income (loss) from continuing operations	(803)	9,095	(1,425)	26,754
Discontinued operations	(17,227)	(13,302)	(27,123)	(29,948)
Net (loss) income	$ (18,030)	$ (4,207)	$ (28,548)	$ (3,194)

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Commercial Banking

The following table shows selected financial information for our commercial banking line of business:

	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
	(Dollars in thousands)			
Selected Income Statement Data:				
Interest income	$ 58,729	$ 58,445	$ 175,984	$ 170,513
Interest expense	(28,740)	(26,507)	(86,517)	(77,302)
Net interest income	29,989	31,938	89,467	93,211
Provision for loan and lease losses	(3,100)	(1,668)	(8,541)	(4,481)
Noninterest income	4,099	4,691	12,234	13,553
Total net revenue	30,988	34,961	93,160	102,283
Operating expense	(23,582)	(23,109)	(70,797)	(66,166)
Income before taxes	7,406	11,852	22,363	36,117
Income taxes	(2,697)	(3,594)	(8,149)	(13,245)
Net income	$ 4,709	$ 8,258	$ 14,214	$ 22,872
Performance Ratios:				
Return on Average Equity	8.05%	14.76%	8.14%	14.38%

	September 30, 2007	December 31, 2006
	(Dollars in thousands)	
Selected Balance Sheet Data at End of Period:		
Assets	$3,131,124	$3,103,547
Securities and short-term investments	63,696	55,116
Loans and leases	2,941,207	2,901,029
Allowance for loan and lease losses	(27,457)	(27,113)
Interest-bearing deposits	2,390,799	2,270,946
Non-interest bearing deposits	385,116	364,434
Shareholder s equity	234,331	241,556
Daily Averages:		
Assets	$3,137,263	$3,143,439
Loans and leases	2,895,985	2,797,853
Allowance for loan and lease losses	(26,761)	(26,175)
Deposits	2,759,638	2,826,446
Shareholder s equity	233,439	218,076
Shareholder s equity to assets	0.00%	6.95%
Selected Operating Data:		
Delinquency ratio	0.41%	0.13%

Overview

Our commercial banking line of business focuses on providing credit, cash management and personal banking products to small businesses and business owners. We offer commercial banking services through our banking subsidiaries, Irwin Union Bank and Trust Company, an Indiana state-chartered commercial bank, and Irwin Union Bank, F.S.B., a federal savings bank.

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The following tables show the geographic composition of our commercial banking loans and our core deposits:

	September 30, 2007			December 31, 2006		
Markets	Loans Outstanding	Percent of Total	Weighted Average Coupon	Loans Outstanding	Percent of Total	Weighted Average Coupon
	(Dollars in thousands)					
Indianapolis	$ 536,525	18.2%	7.4%	$ 561,343	19.3%	7.6%
Western and Central Michigan	475,341	16.2	7.4	519,348	17.9	7.7
Phoenix	470,766	16.0	7.4	452,919	15.6	7.9
Southern Indiana	461,845	15.7	7.1	475,051	16.4	7.2
Las Vegas	186,587	6.3	7.9	154,218	5.3	8.1
Other	810,143	27.6	7.5	738,150	25.5	7.9
Total	$2,941,207	100.0%	7.4%	$2,901,029	100.0%	7.7%

	Core Deposits	Percent of Total	Weighted Average Coupon	Core Deposits	Percent of Total	Weighted Average Coupon
Indianapolis	$ 283,969	11.7%	2.6%	$ 259,835	10.8%	2.4%
Western and Central Michigan	205,602	8.5	3.3	231,666	9.7	3.4
Phoenix	237,583	9.8	3.6	179,502	7.5	3.4
Southern Indiana	739,561	30.5	2.8	630,060	26.3	2.8
Las Vegas	443,733	18.3	4.1	467,708	19.5	4.1
Other	517,855	21.2	3.2	631,268	26.2	3.5
Total	$2,428,303	100.0%	3.2%	$2,400,039	100.0%	3.3%

Net Income

Commercial banking net income totaled $4.7 million during the third quarter of 2007 compared to $8.3 million for the same period in 2006. Year-to-date net income totaled $14.2 million in 2007 compared to net income of $22.9 million in 2006.

Net Interest Income

The following table shows information about net interest income for our commercial banking line of business:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
	(Dollars in thousands)			
Net interest income	$ 29,989	$ 31,938	$ 89,467	$ 93,211
Average interest earning assets	2,997,178	2,964,055	3,035,892	3,055,665
Net interest margin	3.97%	4.27%	3.94%	4.08%

Net interest income was $30 million for the third quarter of 2007, a decrease of 6% over third quarter of 2006. Net interest income year to date in 2007 also decreased 4% over the same period in 2006. The 2007 decline in net interest

income resulted primarily from a change in mix of liabilities toward higher cost deposits as well as a shift in mix of our loan portfolio from higher rate adjustable loans to lower fixed rate loans resulting from the inverted yield curve that has been prevalent over the time periods compared. Net interest margin is computed by dividing net interest income by average interest earning assets. Net interest margin for the three months ended September 30, 2007 was 3.97%, compared to 4.27% for the same period in 2006. Year-to-date net interest margin for 2007 was 3.94%, compared to 4.08% for 2006. The decrease in 2007 margin reflects competitive conditions and unfavorable repricing of loans and deposits.

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Provision for Loan and Lease Losses

The provision in the third quarter of 2007 was $3.1 million compared to $1.7 million for the same period in 2006 The provision increased to $8.5 million during the nine months ending September 30, 2007, compared to a provision of $4.5 million during the same period in 2006. The increased year-to-date provision relates primarily to a loss identified in the first quarter related to a commercial credit in Michigan. With respect to this credit, we believe the borrower will be unable to repay the majority of the loan as we discovered what we believe were misrepresentations about collateral offered for the loan. As such, we took a charge-off of $4.1 million related specifically to this loan during the first quarter. Credit quality at the commercial banking line of business has declined throughout the year, reflecting economic slow down in several of our markets, but is still consistent with our historic experiences.. See further discussion in the Credit Quality section below.

Noninterest Income

The following table shows the components of noninterest income for our commercial banking line of business:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
	(Dollars in thousands)			
Trust fees	$ 566	$ 478	$ 1,680	$ 1,456
Service charges on deposit accounts	1,019	1,086	2,814	3,146
Insurance commissions, fees and premiums	405	368	1,426	1,527
Gain from sales of loans	457	822	1,474	1,834
Loan servicing fees	351	377	1,100	1,141
Amortization & impairment of servicing assets	(268)	(303)	(836)	(838)
Brokerage fees	468	329	1,219	989
Other	1,101	1,534	3,357	4,298
Total noninterest income	$ 4,099	$ 4,691	$ 12,234	$ 13,553

Noninterest income during the three and nine months ended September 30, 2007 decreased 13% and 10%, respectively, over the same periods in 2006. This decline relates primarily to lower gains on sales of loans, lower service charges on deposit accounts and to a loss on sale of other real estate owned (OREO) during 2007.

Operating Expenses

(1) On a full time equivalent basis.

Operating expenses for the three and nine months ended September 30, 2007 totaled $24 million and $71 million, respectively, an increase of 2% and 7% over the same periods in 2006. The increase in operating expenses primarily resulted from increased premises and equipment costs due to our recent office expansions.

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Balance Sheet

Total assets at September 30, 2007 were $3.1 billion, unchanged from December 31, 2006. Earning assets for the nine months ended September 30, 2007 averaged $3.0 billion, unchanged from the same period in 2006. Average core deposits for the third quarter of 2007 totaled $2.4 billion, a decrease of 1% over average core deposits in the second quarter 2007.

Credit Quality

The allowance for loan losses to total loans is 0.93% at September 30, 2007, unchanged from 0.93% at December 31, 2006. Total nonperforming assets were $29 million at September 30, 2007, an increase of $10 million versus year end 2006. Other real estate owned was $8.5 million at September 30, an increase of $4.1 million compared to the year-end 2006 balance. The increase in nonperforming loans is primarily attributable to a single credit in a western market which was placed on non-accrual at quarter-end, but which we believe has limited loss exposure. Nonperforming loans are not significantly concentrated in any industry category, although a greater than average amount of our nonperforming loans are located in our Michigan markets.

The following table shows information about our nonperforming assets in this line of business and our allowance for loan losses.

	September 30, 2007	December 31, 2006
	(Dollars in thousands)	
Nonperforming loans	$ 20,596	$ 14,455
Other real estate owned	8,512	4,423
Total nonperforming assets	$ 29,108	$ 18,878
Nonperforming assets to total assets	0.93%	0.61%
Allowance for loan losses	$ 27,457	$ 27,113
Allowance for loan losses to total loans	0.93%	0.93%

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
	(Dollars in thousands)			
Provision for loan losses	$ 3,100	$ 1,668	$ 8,541	$ 4,481
Net charge-offs	2,118	1,315	8,197	2,621
Net charge-offs to average loans	0.29%	0.19%	0.38%	0.13%

The following table shows the ratio of nonperforming assets to total loans by market for the periods indicated:

Markets	September 30, 2007	December 31, 2006
Indianapolis	0.55%	0.24%
Western and Central Michigan	2.85%	2.72%
Southern Indiana	0.16%	0.14%
Phoenix	0.44%	0.52%
Las Vegas	0.01%	0.00%
Other	1.21%	0.06%
Total	0.99%	0.65%

Commercial Finance

The following table shows selected financial information for our commercial finance line of business for the periods indicated:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
	(Dollars in thousands)			
Selected Income Statement Data:				
Net interest income	$ 13,258	$ 10,417	$ 38,189	$ 30,217
Provision for loan and lease losses	(2,860)	(1,613)	(9,392)	(4,562)
Noninterest income	3,480	2,536	9,218	6,684
Total net revenue	13,878	11,340	38,015	32,339
Operating expense	(7,599)	(6,069)	(22,667)	(17,717)
Income before taxes	6,279	5,271	15,348	14,622
Income taxes	(2,471)	(1,997)	(6,013)	(5,525)
Net income	$ 3,808	$ 3,274	$ 9,335	$ 9,097
Selected Operating Data:				
Net charge-offs	$ 1,651	$ 1,211	$ 5,686	$ 2,826
Net interest margin	4.44%	4.27%	4.59%	4.47%
Total funding of loans and leases	$ 185,478	$ 147,056	$ 488,831	$ 431,537
Return on average equity	13.70%	18.02%	12.14%	17.75%

	September 30, 2007	December 31, 2006
	(Dollars in thousands)	
Selected Balance Sheet Data at End of Period:		
Total assets	$ 1,251,874	$ 1,073,552
Loans and leases	1,234,312	1,056,406
Allowance for loan and lease losses	(16,790)	(13,525)
Shareholders equity	115,728	88,587

Overview

We established this line of business in 1999. We offer commercial finance products and services through a direct subsidiary of our banking subsidiary, Irwin Union Bank and Trust, an Indiana state-chartered commercial bank and its direct and indirect subsidiaries. In this segment, we provide small ticket lease financing on a variety of small business equipment in the United States and Canada as well as equipment and leasehold improvement financing for franchisees (mainly in the quick service restaurant sector) in the United States. In 2006, we expanded our product line to include professional practice financing and information technology leasing to middle and upper middle market companies throughout the United States and Canada.

We provide cost-competitive, service-oriented financing alternatives to small businesses generally and to franchisees. We utilize direct and indirect sales forces to distribute our products. In the small ticket lease channel, with an average lease size of approximately $30 thousand in our portfolio, our sales efforts focus on providing lease solutions for vendors and manufacturers. The majority of our leases are full payout (no residual), small-ticket assets secured by commercial equipment. We finance a variety of commercial, light industrial and office equipment. Within the franchise channel, the financing of equipment and real estate is structured as loans. The loan amounts average

approximately $500 thousand.

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Portfolio Characteristics

The following tables show the geographic composition of our commercial finance loans and leases:

	September 30, 2007	December 31, 2006
United States		
California	11.7%	12.4%
Texas	7.5	5.9
New York	4.1	5.0
New Jersey	4.1	3.5
All other states	40.0	43.3
Total United States	67.4%	70.1%
Canada [(1)]		
Ontario	8.2%	7.3%
British Columbia	7.5	7.0
Quebec	7.4	7.1
Alberta	6.6	5.8
All other provinces	2.9	2.6
Total Canada	32.6%	29.9%
Total	100.0%	100.0%
Total Portfolio	$ 1,234,312	$ 1,056,406

(1) In U.S. dollars

The following table provides certain information about the loan and lease portfolio of our commercial finance line of business at the dates shown:

	September 30, 2007	December 31, 2006
	(Dollars in thousands)	
Domestic franchise loans	$ 567,503	$ 488,489
Weighted average coupon	9.34%	8.79%
Delinquency ratio	0.30	0.16
Domestic leases	$ 264,265	$ 253,274
Weighted average coupon	10.83%	10.32%
Delinquency ratio	2.30	1.72
Canadian leases [(1)]	$ 402,544	$ 314,644
Weighted average coupon	9.16%	9.13%
Delinquency ratio	0.45	0.36

(1) In U.S. dollars.

Net Income

During the three months ended September 30, 2007, the commercial finance line of business recorded net income of $3.8 million, a 15% increase over the $3.3 million earned during the same period in the prior year. Year to date, the commercial finance line of business earned $9.3 million compared to $9.1 million for the same period in the prior year. The 2007 increase in earnings is attributable primarily to higher net interest income related to a larger portfolio as well as higher gains from sales of loans.

Net Interest Income

The following table shows information about net interest income for our commercial finance line of business:

	Three Months September 30,		Nine Months September 30,	
	2007	2006	2007	2006
	(Dollars in thousands)			
Net interest income	$ 13,258	$ 10,417	$ 38,189	$ 30,217
Average interest earning assets	1,184,323	968,008	1,113,288	903,603
Net interest margin	4.44%	4.27%	4.59%	4.47%

Net interest income was $13 million for the quarter ended September 30, 2007, an increase of 27% over 2006. Year-to-date net interest income was $38 million compared to $30 million in 2006. The improvement in net interest income resulted primarily from an increase in our portfolio. The total loan and lease portfolio has increased to $1.2 billion at September 30, 2007, an increase of 17% over year-end 2006 and an increase of 24% over September 30, 2006. This line of business originated $185 million and $489 million in loans and leases during the third quarter and year-to-date 2007, respectively, compared to $147 million and $432 million during the same periods of 2006. The portfolio increased $55 million as of September 30, 2007 relative to December 31, 2006 due solely to the increased value of the Canadian dollar relative to the U.S. dollar.

Net interest margin is computed by dividing net interest income by average interest earning assets. Net interest margin for the third quarter of 2007 was 4.44% compared to 4.27% in 2006 for the same period. Year-to-date margins improved to 4.59% in 2007 compared to 4.47% during the same period in 2006. The increase in 2007 margin is due primarily to higher loan fees.

Provision for Loan and Lease Losses

The provision for loan and lease losses increased to $9.4 million during the first nine months in 2007 compared to $4.6 million for the same period in 2006. The third quarter provision increased to $2.9 million versus $1.6 million during the same period in 2006. The increased provisioning levels relate primarily to losses identified in the domestic small ticket leasing component of the commercial finance portfolio.

Noninterest Income

The following table shows the components of noninterest income for our commercial finance line of business:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
	(Dollars in thousands)			
Gain from sales of loans	$ 1,768	$ 939	$ 4,805	$ 2,191
Derivative (losses) gains, net	(51)	26	(325)	(192)
Other	1,763	1,571	4,738	4,685
Total noninterest income	$ 3,480	$ 2,536	$ 9,218	$ 6,684

Noninterest income during the three months ended September 30, 2007 increased 37% over the same period in 2006. Year-to-date noninterest income was $9.2 million, compared to $6.7 million in the same period of 2006. Included in noninterest income were gains that totaled $1.8 million and $4.8 million for the three and nine months ended September 30, 2007, compared to gains of $0.9 million and $2.2 million during the same periods in 2006. These 2007 gains were the result of whole loan sales of $32 million and $66 million, respectively, for the three and nine-month periods ended September 30, 2007. In addition to whole loan sales, we also sold $2 million and $39 million, respectively, in participations of our franchise loan portfolio during the three and nine-month periods ended September 30, 2007. We had no loan participation sales in 2006.

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Operating Expenses

The following table shows the components of operating expenses for our commercial finance line of business:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
	(Dollars in thousands)			
Salaries and employee benefits	$ 4,629	$ 3,340	$ 14,112	$ 9,921
Other	2,970	2,729	8,555	7,796
Total operating expenses	$ 7,599	$ 6,069	$ 22,667	$ 17,717
Efficiency ratio	45.40%	46.85%	47.81%	48.01%
Number of employees at period end [1]			192	195

(1) On a full time equivalent basis.

Operating expenses during the third quarter and year-to-date in 2007 totaled $7.6 million and $22.7 million, respectively, an increase of 25% and 28% over the same periods in 2006. The increased salaries and benefits expense relates to the continued growth in this business, including compensation costs related to higher production levels, infrastructure and staffing development, as well as incentive compensation costs related to profitability.

Credit Quality

The commercial finance line of business had nonperforming loans and leases at September 30, 2007 of $6.5 million, compared to $5.4 million as of December 31, 2006. The year-over-year increase in nonperforming loans was largely attributable to a decline in credit quality in our domestic lease portfolio. Net charge-offs recorded by this line of business totaled $1.7 million for the third quarter of 2007, compared to $1.2 million for the third quarter of 2006. Net charge-offs year to date were $5.7 million, up from the $2.8 million of net charge-offs recorded year to date in 2006. Our allowance for loan and lease losses at September 30, 2007 totaled $16.8 million, representing 1.36% of loans and leases, compared to a balance at December 31, 2006 of $13.5 million, or 1.28% of loans and leases.

The following table shows information about our nonperforming loans and leases in this line of business and our allowance for loan and lease losses:

	September 30, 2007	December 31, 2006
	(Dollars in thousands)	
Nonperforming loans	$ 6,459	$ 5,374
Allowance for loan losses	16,790	13,525
Allowance for loan losses to total loans	1.36%	1.28%

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
	(Dollars in thousands)			
Provision for loan losses	$ 2,860	$ 1,613	$ 9,392	$ 4,562
Net charge-offs	1,651	1,211	5,686	2,826
Annualized net charge-offs to average loans	0.56%	0.50%	0.69%	0.42%

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Home Equity Lending

The following table shows selected financial information for the home equity lending line of business:

	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
	(Dollars in thousands)		(Dollars in thousands)	
Selected Income Statement Data:				
Net interest income	$ 23,405	$ 25,215	$ 72,442	$ 71,807
Provision for loan and lease losses	(22,533)	(5,854)	(53,222)	(16,111)
Noninterest income	3,208	(820)	1,173	10,149
Total net revenues	4,080	18,541	20,393	65,845
Operating expenses	(17,638)	(19,010)	(54,087)	(65,202)
Income (loss) before taxes	(13,558)	(469)	(33,694)	643
Income taxes	5,420	177	13,456	(283)
Net income (loss)	$ (8,138)	$ (292)	$ (20,238)	$ 360
Selected Operating Data:				
Loan volume:				
Lines of credit	$ 7,554	$ 29,940	$ 27,909	$ 124,859
Loans	96,005	224,250	388,008	625,039
Net home equity charge-offs to average managed portfolio	3.10%	0.86%	2.77%	0.82%
Gain on sale of loans to loans sold	0.94%	0.65%	0.53%	1.16%

	September 30, 2007	December 31, 2006
	(Dollars in thousands)	
Selected Balance Sheet Data:		
Total assets	$1,561,817	$1,617,219
Home equity loans and lines of credit[(1)]	1,500,919	1,280,497
Allowance for loan losses	(59,981)	(33,614)
Home equity loans held for sale	3,732	236,636
Residual interests	3,250	2,760
Mortgage servicing assets	22,047	28,231
Short-term borrowings	281,641	446,163
Collateralized debt	1,013,174	948,939
Shareholders equity	184,007	155,791
Selected Operating Data:		
Total managed portfolio balance	1,653,606	1,708,975
Delinquency ratio[(2)]	4.7%	3.2%
Weighted average coupon rate:		
Lines of credit	11.16%	11.13%
Loans	11.06	10.75

(1)

Includes $1.2 billion and $1.1 billion of collateralized loans at September 30, 2007 and December 31, 2006, respectively, pledged as part of securitized financings.

(2) Nonaccrual loans are included in the delinquency ratio.

Overview

Our home equity lending line of business originates, purchases, sells, and services a variety of mortgage loans nationwide. We offer mortgage products through our banking subsidiary, Irwin Union Bank and Trust, an Indiana state-chartered commercial bank and its direct subsidiary. We market our mortgage loans (generally using second mortgage liens, but also including first mortgage liens) principally through brokers and correspondents, and also through the Internet. We seek to serve creditworthy homeowners who are active credit users.

We offer mortgage loans with combined loan-to-value (CLTV) ratios of up to 125% of their collateral value to borrowers we believe have prime credit-quality. Mortgage loans are priced using a proprietary model, taking into account, among other factors, the credit history of our customer and the relative loan-to-value (LTV) ratio of the loan at origination. For most of our home equity product offerings, we offer customers the choice to accept an early repayment fee in exchange for a lower interest rate. Generally and historically, we either sell loans through whole loan sales or we fund these loans on balance sheet through warehouse lines or secured, term financings. In recent months, the secured, term funding market has been disrupted and, therefore, we have begun funding the loans we retain in portfolio using deposit or other wholesale sources. In an effort to manage portfolio concentration risk and to comply with existing banking regulations, we have policies in place governing the size of our investment in loans secured by real estate where the LTV is greater than 90%.

Production and Portfolio Characteristics

The following table shows the geographic composition of our home equity managed portfolio:

State	September 30, 2007	December 31, 2006
California	9.7%	10.2%
Michigan	7.9	7.8
Colorado	7.6	7.0
Ohio	6.7	6.2
Florida	6.5	7.8
All other states	61.6	61.0
Total	100.0%	100.0%
Total managed portfolio in thousands	$ 1,653,606	$ 1,708,975

For the nine months ended September 30, 2007, loans with loan-to-value ratios greater than 100%, but less than 125% (high LTVs, or HLTVs) constituted 53% of our loan originations. HLTV s represented 54% of our managed portfolio for this line of business at September 30, 2007. In the current environment, there is not an active secondary market for these loans. As such, we have taken steps to limit production of these loans to the amount we can hold in our portfolio. HLTVs constituted 47% of our managed portfolio at December 31, 2006. Approximately 68%, or $1.1 billion, of our home equity managed portfolio at September 30, 2007 was originated with early repayment provisions.

The following table provides a breakdown of our home equity lending managed portfolio by product type, outstanding principal balance and weighted average coupon for the following periods:

	September 30, 2007			December 31,2006		
	Amount	% of Total	Weighted Average Coupon	Amount	% of Total	Weighted Average Coupon
	(Dollars in thousands)					
Loans ≤ 100% CLTV	$ 445,641	26.95%	9.06%	$ 536,387	31.39%	9.10%
Lines of credit ≤ 100% CLTV	259,976	15.72	9.92	319,415	18.69	9.96
	47,813	2.89	7.67	44,727	2.62	7.37

First mortgages ≤ 100% CLTV						
Total ≤ 100% CLTV	753,430	45.56	9.27	900,529	52.70	9.32
Loans > 100% CLTV	781,372	47.25	12.49	677,119	39.62	12.36
Lines of credit > 100% CLTV	89,660	5.42	14.57	101,683	5.95	14.55
First mortgages > 100% CLTV	23,771	1.44	8.48	22,916	1.34	8.48
Total > 100% CLTV	894,803	54.11	12.59	801,718	46.91	12.53
Other (including discontinued products)	5,373	0.33	14.16	6,728	0.39	15.03
Total managed portfolio[(1)]	$ 1,653,606	100.00%	11.08%	$ 1,708,975	100.00%	10.85%

(1) We define our managed portfolio as the portfolio ($1.7 billion) that we service and on which we carry credit risk. At September 30, 2007, we also serviced another $0.8 billion of loans for which the credit risk is held by others.

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The following table shows the composition of our loan volume by categories for the periods indicated:

Product	Three Months Ended September 30,	
	2007	2006
	(Funding amount in thousands)	
First mortgage loans		
Funding Amount	$ 23,416	$ 15,716
Weighted Average Disposable Income	5,526	4,707
Weighted Average FICO score	703	686
Weighted Average Coupon	8.35%	8.43%
First mortgage loans up to 110%		
Funding Amount	$	$ 10,726
Weighted Average Disposable Income		6,872
Weighted Average FICO score		703
Weighted Average Coupon	0.00%	8.53%
Home equity loans up to 100% CLTV		
Funding Amount	$ 15,405	$ 131,859
Weighted Average Disposable Income	5,436	6,788
Weighted Average FICO score	707	705
Weighted Average Coupon	10.68%	11.52%
Home equity loans up to 125% CLTV		
Funding Amount	$ 57,184	$ 65,949
Weighted Average Disposable Income	4,906	4,346
Weighted Average FICO score	700	699
Weighted Average Coupon	13.54%	12.84%
Home equity lines of credit up to 100% CLTV		
Funding Amount	$ 2,297	$ 25,439
Weighted Average Disposable Income	6,890	6,582
Weighted Average FICO score	710	686
Weighted Average Coupon		