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ITLA CAPITAL CORP
Form 10-Q
August 14, 2001

1

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

FORM 10-Q

(Mark One)

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

For the Quarterly Period Ended June 30, 2001

OR

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

For the Transition Period from _____ to _____

Commission File Number 0-26960

ITLA CAPITAL CORPORATION

(Exact Name of Registrant as Specified in its Charter)

Delaware

95-4596322

(State or Other Jurisdiction of
Incorporation or Organization)

(IRS Employer
Identification No.)

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

92037

(Address of Principal Executive Offices)

(Zip Code)

(858) 551-0511

(Registrant's Telephone Number, Including Area Code)

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

Number of shares of common stock of the registrant: 6,143,413 outstanding
as of August 7, 2001.

2

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FORM 10-Q

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FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2001
TABLE OF CONTENTS

PART I -- FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Consolidated Balance Sheets - June 30, 2001 and December 31, 2000.....
Consolidated Statements of Income - Three and Six Months
 Ended June 30, 2001 and 2000.....
Consolidated Statements of Cash Flows -
 Six Months Ended June 30, 2001 and 2000.....
Notes to Unaudited Consolidated Financial Statements.....

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND
RESULTS OF OPERATIONS.....

ITEM 3. MARKET RISK.....

PART II -- OTHER INFORMATION

ITEM 1. Legal Proceedings.....
ITEM 2. Changes in Securities.....
ITEM 3. Defaults Upon Senior Securities.....
ITEM 4. Submission of Matters to a Vote of Security Holders.....
ITEM 5. Other Information.....
ITEM 6. Exhibits and Reports on Form 8-K.....
Signatures.....

FORWARD LOOKING STATEMENTS

"Safe Harbor" statement under the Private Securities Litigation Reform Act of 1995: This Form 10-Q contains forward-looking statements that are subject to risks and uncertainties, including, but not limited to, changes in economic conditions in our market areas, changes in policies by regulatory agencies, the impact of competitive loan products, loan demand risks, fluctuations in interest rates and operating results and other risks detailed from time to time in our filings with the Securities and Exchange Commission. We caution readers not to place undue reliance on forward-looking statements. We do not undertake and specifically disclaim any obligation to revise any forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date of such statements. These risks could cause our actual results for 2001 and beyond to differ materially from those expressed in any forward-looking statements by, or on behalf of, us.

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

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2001
(UNAUDITED)

(IN THOUSANDS EXC

ASSETS

Cash and cash equivalents	\$ 98,301
Investment securities available for sale, at fair value	14,474
Stock in Federal Home Loan Bank	9,307
Real estate loans, net (net of allowance for loan losses of \$22,661 and \$22,608 in 2001 and 2000, respectively)	1,080,332
Real estate loans, held in trust (net of allowance for loan losses of \$4,578 in 2001 and 2000)	184,784
Interest receivable	10,933
Other real estate owned, net	2,124
Premises and equipment, net	2,103
Deferred income taxes	11,137
Other assets	8,025

Total assets	\$ 1,421,520 =====

LIABILITIES AND SHAREHOLDERS' EQUITY

Liabilities:

Deposit accounts	\$ 926,912
Collateralized mortgage obligations	135,154
Federal Home Loan Bank advances	186,135
Accounts payable and other liabilities	11,453

Total liabilities	1,259,654 -----

Commitments and contingencies

Guaranteed preferred beneficial interests in the Company's junior subordinated deferrable interest debentures, net	28,069
--	--------

Shareholders' equity:

Preferred stock, 5,000,000 shares authorized, none issued	--
Contributed capital-common stock, \$.01 par value; 20,000,000 shares authorized, 8,210,749 and 8,206,749 issued and outstanding in 2001 and 2000, respectively	57,168
Retained earnings	107,049
Accumulated other comprehensive income	21

	164,238
Less treasury stock, at cost - 2,058,336 and 1,546,336 shares in 2001 and 2000, respectively	(30,441)

Total shareholders' equity	133,797

Total liabilities and shareholders' equity	\$ 1,421,520 =====

See accompanying notes to the unaudited consolidated financial statements.

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4

ITLA CAPITAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(UNAUDITED)

	FOR THE THREE MONTHS ENDED JUNE 30,		FOR THE END
	(IN THOUSANDS EXCEPT PER SHARE)		
	2001	2000	2001
Interest income:			
Real estate loans, including fees	\$ 26,635	\$ 24,778	\$ 53,418
Real estate loans held in trust	4,006	5,672	8,328
Cash and investment securities	787	1,093	1,948
Total interest income	31,428	31,543	63,694
Interest expense:			
Deposit accounts	14,097	13,389	29,911
Collateralized mortgage obligations	1,689	3,830	3,982
Federal Home Loan Bank advances	1,127	444	1,658
Total interest expense	16,913	17,663	35,551
Net interest income before provision for loan losses	14,515	13,880	28,143
Provision for loan losses	500	1,200	950
Net interest income after provision for loan losses	14,015	12,680	27,193
Noninterest income:			
Fee income from mortgage banking activities	--	33	60
Gain on sale of investment securities available for sale	--	--	--
Other	239	111	493
Total noninterest income	239	144	553
Noninterest expense:			
Compensation and benefits	3,097	2,439	5,853
Occupancy and equipment	750	696	1,443
FDIC assessment	48	47	93
Other	1,886	1,919	3,523
Total recurring general and administrative Nonrecurring expense	5,781	5,101	10,912
Total general and administrative	5,781	5,101	10,912

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Real estate owned expense (income), net	35	6	50
Provision for losses on other real estate owned	81	--	203
(Gain) loss on sale of other real estate owned, net	(69)	(60)	(37)
	-----	-----	-----
Total real estate owned expense, net	47	(54)	216
	-----	-----	-----
Total noninterest expense	5,828	5,047	11,128
	-----	-----	-----
Income before provision for income taxes and minority interest in income of subsidiary	8,426	7,777	16,618
Minority interest in income of subsidiary	796	--	1,370
	-----	-----	-----
Income before provision for income taxes	7,630	7,777	15,248
Provision for income taxes	2,911	3,184	5,816
	-----	-----	-----
NET INCOME	\$ 4,719	\$ 4,593	\$ 9,432
	=====	=====	=====
BASIC EARNINGS PER SHARE	\$ 0.71	\$ 0.64	\$ 1.41
	=====	=====	=====
DILUTED EARNINGS PER SHARE	\$ 0.69	\$ 0.63	\$ 1.36
	=====	=====	=====

See accompanying notes to the unaudited consolidated financial statements.

4

5

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

	FOR THE S
	J

	2001

	(IN
Cash Flows From Operating Activities:	
Net Income	\$ 9,432
Adjustments to reconcile net income to net cash provided by operating activities:	
Depreciation and amortization of premises and equipment	405
Amortization of premium on purchased loans	1,615
Accretion of deferred loan origination fees, net of costs	(915)
Amortization of original issue discount and deferred debt issuance costs on collateralized mortgage obligations	166
Provision for loan losses	950
Provision for losses on other real estate owned	203
Gain on sale of investment securities available for sale	--
(Gain) loss in the sale of other real estate owned	(37)

5

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Decrease (increase) in interest receivable	888
Decrease (increase) in other assets	244
Increase in accounts payable and other liabilities	185

Net cash provided by operating activities	13,136

Cash Flows From Investing Activities:	
Purchases of investment securities available for sale	(11,000)
Proceeds from maturity of investment securities available for sale	43,260
Proceeds from the sale of investment securities available for sale	--
(Increase) decrease in stock in Federal Home Loan Bank	(5,344)
Purchases of real estate loans	(119,852)
Decrease in real estate loans, net	82,488
Cash paid to acquire ICCMAC Multifamily and Commercial Trust 1999-1	--
Repayment of real estate loans held in trust	26,118
Proceeds from sale of real estate loans	356
Proceeds from the sale of other real estate owned	1,723
Other, net	(198)

Net cash provided by (used in) investing activities	17,551

Cash Flows From Financing Activities:	
Net (decrease) increase in deposit accounts	(88,787)
Principal repayments on collateralized mortgage obligations	(26,864)
Proceeds from borrowings from the Federal Home Loan Bank	106,885
Repayment of borrowings from the Federal Home Loan Bank	--
Proceeds from the issuance of trust preferred securities	14,549
Proceeds from exercise of employee stock options	48
Cash paid to acquire treasury stock	(9,167)

Net cash used in financing activities	(3,336)

Net increase (decrease) in cash and cash equivalents	27,351
Cash and cash equivalents at beginning of the period	70,950

Cash and cash equivalents at end of period	\$ 98,301
	=====
Supplemental Cash Flow Information:	
Cash paid during the period for interest	\$ 35,729
Cash paid during the period for income taxes	\$ 5,800
Noncash Investing Transactions:	
Loans transferred to other real estate owned	\$ 1,773

See accompanying notes to the unaudited consolidated financial statements

ITLA CAPITAL CORPORATION AND SUBSIDIARIES

NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - BASIS OF PRESENTATION

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The unaudited consolidated financial statements of ITLA Capital Corporation ("the Company") included herein reflect all normal recurring adjustments which are, in the opinion of management, necessary to present a fair statement of the results for the interim period indicated. The unaudited consolidated financial statements include the accounts of ITLA Capital and its subsidiaries, Imperial Capital Bank (the "Bank") and Imperial Capital Real Estate Investment Trust ("Imperial Capital REIT"), ITLA Capital Statutory Trust I ("Trust I") and ITLA Capital Statutory Trust II ("Trust II"). All intercompany transactions and balances have been eliminated. Certain information and disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to the rules and regulations of the U.S. Securities and Exchange Commission. The results of operations for the three and six months ended June 30, 2001 are not necessarily indicative of the results of operations for the remainder of the year.

These unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in our annual report on Form 10-K for the year ended December 31, 2000.

NOTE 2 - EARNINGS PER SHARE

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

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

	FOR THE THREE MONTHS ENDED JUNE 30,			FOR THE SIX MONTHS ENDED JUNE 30,	
	NET INCOME	WEIGHTED- AVERAGE SHARES OUTSTANDING	PER SHARE AMOUNT	NET INCOME	WEIGHTED- AVERAGE SHARES OUTSTANDING
	(IN THOUSANDS, EXCEPT PER SHARE DATA)				
2001					
Basic EPS	\$4,719	6,633	\$ 0.71	\$9,432	6,676
Effect of dilutive stock options	--	221	(0.02)	--	236
Diluted EPS	\$4,719	6,854	\$ 0.69	\$9,432	6,912
2000					
Basic EPS	\$4,593	7,190	\$ 0.64	\$8,837	7,206
Effect of dilutive stock options	--	114	(0.01)	--	112
Diluted EPS	\$4,593	7,304	\$ 0.63	\$8,837	7,318

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6

7

NOTE 3 - COMPREHENSIVE INCOME

Comprehensive income, which encompasses net income and the net change in unrealized gains (losses) on investment securities available for sale, is presented below:

	THREE MONTHS ENDED JUNE 30,		SIX MO J
	----- 2001 -----	2000 -----	----- 2001 -----
	(IN THOUSANDS)		
Net Income	\$ 4,719	\$ 4,593	\$ 9,432
Other comprehensive income (loss)- Unrealized gain (loss) on investment securities available for sale, net of tax expense of \$20 and \$28 for the three months ended June 30, 2001 and 2000, and net of tax benefit of \$47 and \$1 for the six months ended June 30, 2001 and 2000, respectively.	30	70	(70)
Less: reclassification adjustment for gains included in net income, net of tax benefit of \$578 in 2000	--	--	--
Comprehensive income	----- \$ 4,749 =====	----- \$ 4,663 =====	----- \$ 9,362 =====

NOTE 4 - IMPAIRED LOANS RECEIVABLE

As of June 30, 2001 and December 31, 2000, the recorded investment in impaired real estate loans and impaired real estate loans held in trust was \$28.3 million and \$18.9 million, respectively. The average recorded investment in impaired loans was \$28.5 million for the three months ended June 30, 2001 and \$13.3 million for the same period last year. The average recorded investment in impaired loans was \$25.2 million for the six months ended June 30, 2001 and \$16.0 million for the same period last year. Interest income recognized on impaired loans totaled \$12,000 for the three and six months ended June 30, 2001 as compared to none and \$300,000 for the same periods last year.

NOTE 5 - GUARANTEED PREFERRED BENEFICIAL INTERESTS IN COMPANY'S JUNIOR SUBORDINATED DEFERRABLE INTEREST DEBENTURES

The Company has two wholly-owned trust subsidiaries, Trust I and Trust II which issued \$14.0 million of 10.60% cumulative trust preferred securities and \$15.0 million of 10.20% cumulative trust preferred securities, respectively, referred to collectively as the Trust Preferred securities. ITLA Capital has fully and unconditionally guaranteed the Trust Preferred securities along with all obligations of each trust under their respective trust agreements. Each trust was formed for the exclusive purpose of issuing their respective Trust Preferred securities and common securities and using the proceeds to acquire ITLA Capital's junior subordinated deferrable interest debentures. Trust I acquired an aggregate principal amount of \$14.4 million of ITLA Capital's 10.60%

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junior subordinated deferrable interest debentures due September 7, 2030 and Trust II acquired an aggregate principal amount of \$15.5 million of ITLA Capital's 10.20% junior subordinated deferrable interest debentures due February 22, 2031. The sole assets of each trust are the debentures it holds. Each of the debentures is redeemable, in whole or in part, at ITLA Capital's option on or after ten years after issuance, at declining premiums to maturity. The Company used the proceeds from the debentures for general corporate purposes, including an aggregate of \$28.0 million in capital contributions to the Bank to support future growth. The costs associated with the Trust Preferred securities issuance have

7

8

been capitalized and are being amortized using a method that approximates the interest method over a period of ten years. The distributions payable on the Trust Preferred securities are reflected as "Minority interest in income of subsidiary" in the Consolidated Statements of Income. The Trust preferred securities are reflected on the Consolidated Statement of Financial Condition as "Guaranteed Preferred Beneficial Interests in the Company's Junior Subordinated Deferrable Interest Debentures."

NOTE 6 - NEW ACCOUNTING PRONOUNCEMENT

The Financial Accounting Standards Board ("FASB") has finalized new accounting standards covering business combinations, goodwill and intangible assets. These new rules published in July 2001, consist of Statement of Financial Accounting Standards ("SFAS") No. 141, "Business Combinations" and SFAS No. 142, "Goodwill and Other Intangible Assets". In conjunction with these new accounting standards the FASB has issued "Transition Provisions for New Business Combination Accounting Rules" ("Provisions") that require the Company to cease amortization of goodwill and adopt the new impairment approach as of January 1, 2002. Management does not expect SFAS No.'s 141 and 142 to have a material effect on the Company's financial condition or results of operations.

ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis is intended to identify the major factors that influenced the financial condition and results of operations for the three months and six months ended June 30, 2001.

RESULTS OF OPERATIONS

THREE MONTHS ENDED JUNE 30, 2001 COMPARED TO THREE MONTHS ENDED JUNE 30, 2000

GENERAL

Consolidated net income totaled \$4.7 million for the three months ended June 30, 2001 compared to \$4.6 million for the same period last year, an increase of 2.2%. The increase in net income was primarily due to the increase in net interest income and the decrease in the provision for loan losses, partially offset by increases in noninterest expense and the expense associated with the Trust Preferred securities. Diluted EPS was \$0.69 for the three months ended June 30, 2001 compared to \$0.63 for the same period last year, an increase of 9.5%.

The return on average assets was 1.37% for the three months ended June 30, 2001 compared to 1.45% for the same period last year. The return on average shareholders' equity was 13.69% for the three months ended June 30, 2001,

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compared to 14.50% for the same period last year.

Total loan production was \$118.1 million for the three months ended June 30, 2001, consisting of the origination and/or purchase of \$99.4 million of commercial real estate loans, \$2.5 million of residential real estate loans and \$16.2 million of franchise loans. Loan production during the same period last year totaled \$74.6 million, consisting of the origination of \$37.1 million of commercial real estate loans and the purchase of \$37.5 million of residential real estate loans.

8

9

NET INTEREST INCOME AND MARGIN

The following table presents, for the three months ended June 30, 2001 and 2000, our condensed average balance sheet information, together with interest income and yields earned on average interest-earning assets and interest expense and rates paid on average interest-bearing liabilities. Average balances are computed using daily average balances. Nonaccrual loans are included in loans receivable.

	FOR THE THREE MONTHS ENDED JUNE 30,				
	2001			2000	
	AVERAGE BALANCE	INCOME/ EXPENSE	YIELD/ RATE	AVERAGE BALANCE	INCOME/ EXPENSE
	(DOLLARS IN THOUSANDS)				
ASSETS					
Cash and investments	\$ 63,279	\$ 787	4.99%	\$ 66,714	\$
Loans receivable:					
Real estate loans	1,114,223	26,635	9.59%	947,193	
Real estate loans held in trust	195,059	4,006	8.24%	255,339	
Total loans receivable	1,309,282	30,641	9.39%	1,202,532	
Total interest-earning assets	1,372,561	\$ 31,428	9.18%	1,269,246	\$
Noninterest-earning assets	32,345			27,254	
Allowance for loan losses	(27,401)			(24,780)	
Total assets	\$ 1,377,505			\$ 1,271,720	
LIABILITIES AND SHAREHOLDERS' EQUITY					
Deposit accounts:					
Money market and passbook accounts	\$ 105,619	\$ 1,139	4.33%	\$ 115,418	\$
Time certificates	860,915	12,958	6.04%	781,635	
Total deposit accounts	966,534	14,097	5.85%	897,053	

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Collateralized mortgage obligations	140,575	1,689	4.82%	201,758	
FHLB advances	89,164	1,127	5.07%	31,931	
	-----	-----	----	-----	-----
Total interest-bearing liabilities	1,196,273	\$ 16,913	5.67%	1,130,742	\$
		=====	=====		=====
Noninterest-bearing liabilities	14,934			13,542	
Trust preferred securities	28,063			--	
Shareholders' equity	138,235			127,436	
	-----			-----	
Total liabilities and shareholders' equity	\$ 1,377,505			\$ 1,271,720	
	=====			=====	
Net interest spread			3.51%		
			=====		
Net interest income					
Before provision for loan losses		\$ 14,515			\$
		=====			=====
Net interest margin			4.24%		
			=====		

9

10

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

	FOR THE THREE MONTHS ENDED JUNE 30, 2001 AND 2000 INCREASE (DECREASE) DUE TO:		
	VOLUME	RATE	TOTAL
	-----	-----	-----
	(IN THOUSANDS)		
Interest and fees earned from:			
Real estate loans	\$ 4,032	\$ (2,175)	\$ 1,857
Real estate loans held in trust	(1,230)	(436)	(1,666)
Cash and investment securities	(42)	(264)	(306)
	-----	-----	-----
Total increase (decrease) in interest income	\$ 2,760	(2,875)	(115)
	-----	-----	-----
Interest paid on:			
Deposit accounts	1,036	(328)	708
Collateralized mortgage obligations	(733)	(1,408)	(2,141)
FHLB advances	724	(41)	683
	-----	-----	-----
Total increase (decrease) in			

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interest expense	1,027	(1,777)	(750)
	-----	-----	-----
Increase (decrease) in net interest income	\$ 1,733	\$ (1,098)	\$ 635
	=====	=====	=====

Total interest income decreased \$115,000 to \$31.4 million in the second quarter of 2001 compared to \$31.5 million for the same period last year. The decrease in interest income was due primarily to lower yields on interest earning assets partially offset by an increase in interest income due to a higher average outstanding balance of interest earning assets.

The average balance of real estate loans was \$1.1 billion for the three months ended June 30, 2001 as compared to \$947.2 million for the same period last year. This increase was primarily due to increases in real estate loans secured by income producing properties, construction loans and purchased single family residential mortgages. Loans secured by income producing properties and construction loans had an average balance of \$977.7 million during the quarter ended June 30, 2001 compared to \$839.4 million during the same period last year. The average balance of purchased single family residential mortgages was \$136.5 million during the quarter ended June 30, 2001, compared to \$107.8 million in the same period in the prior year. Purchased single family residential mortgages are not presently expected to materially increase as a percentage of our current total assets. The average balance of real estate loans held in trust was \$195.1 million for the three months ended June 30, 2001 as compared to \$255.3 million for the same period last year. This decrease was primarily due to loan prepayments and principal amortization.

The average yield earned on real estate loans decreased 93 basis points to 9.59% in the quarter ended June 30, 2001 as compared to 10.52% in the same period last year. The decrease in the yield on real estate loans was primarily due to the repricing of variable rate loans at lower interest rates resulting from the general decline in market interest rates. Our commercial real estate loan portfolio is primarily comprised of adjustable rate mortgages indexed to the six month LIBOR.

Approximately 90.2% of our real estate loan portfolio (including real estate loans held in trust) are adjustable rate mortgages at June 30 2001. These adjustable rate mortgages generally reprice on a quarterly basis and approximately \$1.1 billion or 95.1% of our real estate loan portfolio contain interest rate floors, below which the loans' contractual interest rate may not adjust. At June 30, 2001, the weighted average floor interest rate of these loans was 9.1%. At that date, approximately \$801.6 million or 73.2% of those loans were at the floor interest rate, approximately \$70.3 million or 6.4% were within 50 basis points of their floor interest rate, and approximately \$58.6 million or 5.3% were greater than 50 but less than 100 basis points from their floor interest rate. As market interest rates decline and the loans reprice, more of our portfolio will reach the floor interest rate and no longer reprice downward. Accordingly, we expect that the rate of decline in the yield on our adjustable rate loans due to falling interest rates may be less significant during the remainder of 2001, as compared to the six months ended June 30, 2001.

Total interest expense decreased by \$750,000 to \$16.9 million in the second quarter of 2001, compared to \$17.7 million for the same period last year. This decrease was primarily attributable to lower interest rates paid on all interest bearing liabilities and a lower average balance on the Collateralized Mortgage Obligations ("CMO's") partially offset by higher average balances on

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deposit accounts and Federal Home Loan Bank ("FHLB") advances.

The average balance of deposit accounts increased \$69.4 million to \$966.5 million for the three months ended June 30, 2001 compared to \$897.1 million for the same period last year. Our cost of funds decreased to 5.67% during the three month period ended June 30, 2001, compared to 6.28% for the same period last year. This decrease in funding costs was due primarily to lower rates being paid on the CMO's and deposit accounts as compared to the same period last year due to the general decline in market interest rates. We expect the cost of funds of our deposit accounts to decline during the remainder of 2001, as the certificates issued at higher market interest rates mature and are replaced with certificates that bear interest at current market rates. Approximately \$481.5 million, or 51.9% of our deposit accounts are certificates that will mature within the next six months. The average balance of the CMO's was \$140.6 million during the second quarter of 2001, compared to \$201.8 million for the same period last year. The average rate paid on the CMO's was 4.82% during the three months ended June 30, 2001 compared to 7.63% for the same period last year. FHLB advances averaged \$89.2 million in the current quarter, compared to \$31.9 million for the same period last year.

Net interest margin decreased to 4.24% for the three months ended June 30, 2001 as compared to 4.40% for the same period last year primarily due to the 82 basis point decrease in the yield on total average interest earning assets partially offset by the 61 basis point decrease in cost of funds.

PROVISION FOR LOAN LOSSES

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

- general portfolio trends relative to asset and portfolio size;
- asset categories;
- credit and geographic concentrations;
- delinquency trends and nonaccrual loan levels;
- historical loss experience and risks associated with changes in economic, social and business conditions.

Accordingly, the calculation of the adequacy of the allowance for loan losses is not based solely on the level of nonperforming assets. Management believes that the allowance for loan losses as of June 30, 2001 was adequate to absorb the known and inherent risks of loss in the loan portfolio at that date. While management believes the estimates and assumptions used in its determination of the adequacy of the allowance are reasonable, there can be no assurance that such estimates and assumptions will not be proven incorrect in the future, or that the actual amount of future provisions will not exceed the amount of past provisions or that any increased provisions that may be required will not adversely impact our financial condition and results of operations. In addition, the determination of the amount of the Bank's allowance for loan losses is subject to review by the Bank's regulators, as part of the routine examination process, which may result in the establishment of additional reserves based upon their judgment of information available to them at the time

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of their examination.

The provision for loan losses totaled \$500,000 in the second quarter of 2001, compared to \$1.2 million for the same period in the prior year. The provision for loan losses is recorded to provide for reserves based on the aggregate amount of nonperforming loans and other loans of concern, which has declined in total since December 31, 2000. The allowance for loan losses was 2.11% of total real estate loans and real estate loans held in trust at June 30, 2001 as compared to 2.12% at December 31, 2000. See also-"Financial Condition-Credit Risk."

NONINTEREST EXPENSE

Noninterest expense totaled \$5.8 million for the three months ended June 30, 2001, compared to \$5.0 million for the same period last year. Compensation and benefits expense totaled \$3.1 million during the three months ended June 30, 2001, compared to \$2.4 million for the same period last year. The increase in compensation and benefits expense was primarily due to additions made to retail and wholesale loan origination sales staff.

For the three months ended June 30, 2001, our ratio of consolidated general and administrative expense to average assets, on an annualized basis, increased to 1.68% compared to 1.60% for the same period last year. Our efficiency ratio, (excluding real estate operations), which is defined as general and administrative expenses as a percentage of net interest income and noninterest income was 39.18% for the quarter ended June 30, 2001 compared to 36.37% for the same period last year.

MINORITY INTEREST IN INCOME OF SUBSIDIARY

Minority interest in income of subsidiary was \$796,000 during the three month period ended June 30, 2001 consisting of accrued distributions payable on our Trust Preferred securities. See Note 5 to the unaudited Consolidated Financial Statements for further information.

SIX MONTHS ENDED JUNE 30, 2001 COMPARED TO SIX MONTHS ENDED JUNE 30, 2000

GENERAL

Consolidated net income totaled \$9.4 million for the six months ended June 30, 2001 compared to \$8.8 million for the same period last year, an increase of 6.8%. The increase in net income was primarily due to an increase in net interest income and decreases in noninterest expense and provision for loan losses. These items were partially offset by a decrease in noninterest income and an increase in minority interest in income of subsidiary. Diluted EPS was \$1.36 for the six months ended June 30, 2001 compared to \$1.21 for the same period last year, an increase of 12.4%.

The return on average assets was 1.38% for the six months ended June 30, 2001 compared to 1.51% for the same period last year. The return on average shareholders equity was 13.87% for the six months ended June 30, 2001, compared to 13.97% for the same period last year.

Total loan production was \$247.4 million for the six months ended June 30, 2001, consisting of the origination and/or purchase of \$200.1 million of commercial real estate loans, \$17.8 million of residential real estate loans and \$29.5 million of franchise loans. Loan production during the same period last

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year totaled \$104.5 million, consisting of the origination of \$51.8 million of commercial real estate loans and the purchase of \$52.7 million of residential real estate loans. Additionally, during the same period last year, we acquired \$250.5 million of commercial real estate loans when we purchased the ICCMAC Multifamily and Commercial Trust 1999-1 ("ICCMAC Trust").

13

14

NET INTEREST INCOME AND MARGIN

The following table presents, for the six months ended June 30, 2001 and 2000, our condensed average balance sheet information, together with interest income and yields earned on average interest-earning assets and interest expense and rates paid on average interest-bearing liabilities. Average balances are computed using daily average balances. Nonaccrual loans are included in loans receivable.

	FOR THE SIX MONTHS ENDED JUNE 30,				
	2001			2000	
	AVERAGE BALANCE	INCOME/ EXPENSE	YIELD/ RATE	AVERAGE BALANCE	INCOME/ EXPENSE
	(DOLLARS IN THOUSANDS)				
ASSETS					
Cash and investments	\$ 71,581	\$ 1,948	5.49%	\$ 93,903	\$
Loans receivable:					
Real estate loans	1,094,841	53,418	9.84%	949,008	
Real estate loans held in trust	202,218	8,328	8.30%	133,361	
	1,297,059	61,746	9.60%	1,082,369	
Total loans receivable					
Total interest-earning assets	1,368,640	\$ 63,694	9.38%	1,176,272	\$
		=====	=====		=====
Noninterest-earning assets	32,854			23,680	
Allowance for loan losses	(27,451)			(22,443)	
	\$ 1,374,043			\$ 1,177,509	
	=====			=====	
LIABILITIES AND SHAREHOLDERS' EQUITY					
Deposit accounts:					
Money market and passbook accounts	\$ 105,319	\$ 2,491	4.77%	\$ 120,573	\$
Time certificates	882,750	27,420	6.26%	781,335	
	988,069	29,911	6.10%	901,908	
Collateralized mortgage obligations	147,731	3,982	5.44%	108,574	
FHLB advances	62,300	1,658	5.37%	32,635	
	1,198,100	\$ 35,551	5.98%	1,043,117	\$
Total interest-bearing liabilities					

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	=====	=====	=====
Noninterest-bearing liabilities	14,909		7,141
Trust preferred securities	23,887		--
Shareholders' equity	137,147		127,251
	-----		-----
Total liabilities and shareholders' equity	\$ 1,374,043		\$ 1,177,509
	=====		=====
Net interest spread		3.40%	
		=====	
Net interest income before provision for loan losses	\$ 28,143		\$
	=====		=====
Net interest margin		4.15%	
		=====	

14

15

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

	FOR THE SIX MONTHS JUNE 30, 2001 AND	
	----- INCREASE (DECREASE) -----	
	VOLUME	RATE
	-----	-----
	(IN THOUSANDS)	
Interest and fees earned from:		
Real estate loans	\$ 7,003	\$ (2,964)
Real estate loans held in trust	2,822	(412)
Cash and investments	(615)	(202)
	-----	-----
Total increase (decrease) in interest income	\$ 9,210	(3,578)
	-----	-----
Interest paid on:		
Deposit accounts	2,556	965
Collateralized mortgage obligations	1,048	(1,047)
FHLB advances	787	(23)
	-----	-----
Total increase (decrease) in interest expense	4,391	(105)
	-----	-----
Increase (decrease) in net interest income	\$ 4,819	\$ (3,473)
	=====	=====

16

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Total interest income increased \$5.6 million to \$63.7 million in the six months ended June 30, 2001 compared to \$58.1 million for the same period last year due to increases in the average balance of the Bank's real estate loans and real estate loans held in trust. These increases in interest income were primarily offset by decreases resulting from lower yields on all earning assets and to a lesser extent, the decline in the average balance of cash and investment securities.

The average balance of real estate loans increased to \$1.1 billion during the six months ended June 30, 2001 as compared to \$949.0 million for the same period last year. This increase was primarily due to growth in real estate loans secured by income producing properties, construction loans and purchased single family residential mortgages. Loans secured by income producing properties and construction loans had an average balance of \$959.6 million during the six months ended June 30, 2001 compared to \$851.1 million during the same period last year. The average balance of purchased single family residential mortgages was \$135.3 million during the six months ended June 30, 2001, compared to \$98.0 million during the same period in the prior year. Purchased single family residential mortgages are not presently expected to materially increase as a percentage of our current total assets.

The average balance of real estate loans held in trust was \$202.2 million for the six months ended June 30, 2001 as compared to \$133.4 million for the same period last year. This increase was primarily due to the timing of the acquisition of the ICCMAC Trust which occurred during the last week of the prior years' first quarter.

The average yield earned on real estate loans decreased 62 basis points to 9.84% for the six months ended June 30, 2001 as compared to 10.46% in the same period in the prior year. The decrease in the yield on real estate loans was primarily due to the repricing of variable rate loans at lower interest rates and the reduced yield earned on current period loan production, both resulting from the general decline in market interest rates. Our commercial real estate loan portfolio and

15

16

current loan production is primarily comprised of adjustable rate mortgages indexed to the six month LIBOR.

Total interest expense increased by \$4.3 million to \$35.6 million in the six months ended June 30, 2001, compared to \$31.3 million for the same period last year. This increase was primarily attributable to the increase in the net average balance of deposit accounts, CMO's and FHLB advances.

The average balance of deposit accounts increased \$86.2 million to \$988.1 million for the six months ended June 30, 2001 compared to \$901.9 million for the same period last year. Our cost of funds decreased to 5.98% for the six month period ended June 30, 2001, compared to 6.03% for the same period last year. This decrease in funding costs was due primarily to lower rates paid on the CMO's and FHLB advances, partially offset by higher rates paid on deposit accounts. FHLB advances averaged \$62.3 million for the six months ended June 30, 2001, compared to \$32.6 million for the same period last year. The average rate paid on FHLB advances was 5.37% for the six months ended June 30, 2001, compared to 5.51% for the same period last year. The average balance of the CMO's was \$147.7 million during the six months ended June 30, 2001, compared to \$108.6 million for the same period last year. The average rate paid on the CMO's was

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5.44% during the six months ended June 30, 2001 compared to 7.37% for the same period last year.

Net interest margin decreased to 4.15% for the six months ended June 30, 2001 as compared to 4.58% for the same period last year primarily due to the 55 basis point decrease in the yield on total average interest earning assets and 5 basis point decrease in cost of funds.

PROVISION FOR LOAN LOSSES

The provision for loan losses totaled \$950,000 in the six months ended June 30, of 2001, compared to \$1.8 million for the same period in the prior year. The provision for loan losses is recorded to provide for reserves based on the aggregate amount of nonperforming loans and other loans of concern, which has declined in total since December 31, 2000.

NONINTEREST INCOME

Noninterest income totaled \$553,000 for the six months ended June 30, 2001, compared to \$1.7 million for the same period last year. The previous year's noninterest income included a \$1.4 million gain on sale of investment securities available for sale.

NONINTEREST EXPENSE

Noninterest expense totaled \$11.1 million for the six months ended June 30, 2001, compared to \$11.9 million for the same period last year. The previous year's noninterest expense included a \$1.4 million nonrecurring charge relating to the consolidation of the Bank's headquarters with ITLA Capital's headquarters in La Jolla, California. Compensation and benefits expense totaled \$5.9 million during the six months ended June 30, 2001, compared to \$4.9 million for the same period last year. The increase in compensation and benefits expense was primarily due to additions made to the retail and wholesale loan originations sales staff. In addition, full time equivalent associates totaled 130 for the six months ended June 30, 2001, compared to 115 for the same period last year.

For the six months ended June 30, 2001, our ratio of consolidated general and administrative expense to average assets, on an annualized basis, decreased to 1.59% compared to 1.76% for the same period last year. Our efficiency ratio (excluding real estate operations) which is defined as general

16

17

and administrative expenses as a percentage of net interest income and noninterest income was 38.03% for the six months ended June 30, 2001 compared to 36.35% for the same period last year.

MINORITY INTEREST IN INCOME OF SUBSIDIARY

Minority interest in income of subsidiary was \$1.4 million during the six month period ended June 30, 2001 consisting of accrued distributions payable on our Trust Preferred securities. See Note 5 to the unaudited Consolidated Financial Statements for further information.

FINANCIAL CONDITION

Total assets remained relatively constant at \$1.42 billion at June 30, 2001 and December 31, 2000, respectively. During the six months ended June 30, 2001, the Bank's loan portfolio increased \$34.4 million and, cash and cash

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equivalents increased by \$27.4 million. These increases were partially offset by a \$31.9 million decrease in investment securities available for sale and a \$26.9 million decrease in real estate loans held in trust. Total deposit accounts, which are concentrated in time certificates, decreased to \$926.9 million at June 30, 2001 as compared to \$1.02 billion at December 31, 2000. We retained a majority of the funds which matured through rollover of maturing deposit accounts during the six months ended June 30, 2001 during a sharply declining interest rate environment. Although we compete for deposits primarily on the basis of rates, management believes that a significant portion of deposits will remain with us upon maturity based on our historical experience regarding retention of deposits. CMO's decreased \$26.7 million to \$135.2 million at June 30, 2001 compared to \$161.9 million at December 31, 2000. FHLB advances increased \$106.8 million to \$186.1 million at June 30, 2001, compared to \$79.3 million at December 31, 2000, as we replaced higher costing deposits with lower cost FHLB advances.

17

18

CREDIT RISK

NONPERFORMING ASSETS, OTHER LOANS OF CONCERN AND ALLOWANCE FOR LOAN LOSSES

The following table sets forth our nonperforming assets by category, accruing loans past due 90 days or more and troubled debt restructurings as of the dates indicated.

	JUNE 30, 2001	DECEMBER 31, 2000
	-----	-----
	(DOLLARS IN THOUSANDS)	
Nonaccrual loans:		
Real estate(1)	\$13,294	\$ 9,430
Construction	13,725	8,712
	-----	-----
Total nonaccrual loans	27,019	18,142
Other real estate owned, net	2,124	2,250
	-----	-----
Total nonperforming assets	29,143	20,392
Accruing loans past due 90 days or more with respect to principal or interest	269	9,765
Performing troubled debt restructuring	3,607	3,002
	-----	-----
	\$33,019	\$33,159
	=====	=====
Nonaccrual loans to total real estate loans and real estate loans held in trust	2.11%	1.42%
Allowance for loan losses to nonaccrual loans	100.80%	149.85%
Nonperforming assets to total assets	2.05%	1.44%

(1) Includes one loan with a net book balance of \$225,000 at June 30, 2001 and one loan with a net book of \$1.4 million at December 31, 2000 that are

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nonperforming troubled debt restructurings.

At June 30, 2001, other real estate owned consisted of three income producing properties totaling \$1.7 million and seven single family residential properties totaling \$391,000.

As of June 30, 2001 and December 31, 2000, other loans of concern totaled \$33.9 million and \$70.9 million, respectively. Other loans of concern consist of loans with respect to which known information concerning possible credit problems with the borrowers or the cash flows of the properties securing the respective loans has caused management to be concerned about the ability of the borrowers to comply with present loan repayment terms, which may result in the future inclusion of such loans in the nonaccrual category. The decrease in other loans of concern for the six months ended June 30, 2001 was primarily due to \$15.4 million of loans being paid-off, \$16.9 million of loans being upgraded due to improving conditions and \$10.0 million of loans migrating to nonaccrual status, partially offset by \$5.3 million of new other loans of concern.

Our loan delinquencies (delinquent loans greater than 30 days) increased slightly to \$46.0 million or 3.57% of gross loan portfolio at June 30, 2001 as compared to \$44.1 million or 3.46% of gross loan portfolio at December 31, 2000.

18

19

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

	FOR SIX MONTHS ENDED JUNE 30, 2001	FOR THE YEAR ENDED DECEMBER 31, 2000
	-----	-----
	(DOLLARS IN THOUSANDS)	
Balance at beginning of period	\$ 27,186	\$ 19,895
Provision for loan losses	950	4,775
Addition due to purchase of the ICCMAC Trust	--	4,614
Charge-offs:		
Real estate loans	(918)	(1,489)
Construction loans	--	(1,000)
	-----	-----
Total charge-offs	(918)	(2,489)
	-----	-----
Recoveries:		
Real estate loans	21	391
	-----	-----
Total recoveries	21	391
	-----	-----
Net charge-offs	(897)	(2,098)
	-----	-----

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Balance at end of period	\$ 27,239 =====	\$ 27,186 =====
Allowance for loan losses as a percentage of real estate loans and loans held in trust, net	2.11%	2.12%

LIQUIDITY

Liquidity refers to our ability to maintain cash flow adequate to fund operations and meet obligations and other commitments on a timely basis, including the payment of maturing deposits and the origination or purchase of new real estate loans. We maintain a cash and investment securities portfolio designed to satisfy operating liquidity requirements while preserving capital and maximizing yield. As of June 30, 2001, we held approximately \$98.3 million of cash and cash equivalents (consisting primarily of short-term investments with original maturities of 90 days or less) and \$14.5 million of investment securities classified as available for sale. Short-term fixed income investments classified as cash equivalents consisted of interest-bearing deposits at financial institutions, government money market funds and short-term government agency securities, while investment securities available for sale consisted primarily of fixed income instruments which were rated "AAA" or equivalent by nationally recognized rating agencies. As of June 30, 2001 and December 31, 2000, the Bank's liquidity ratios were 12.1% and 11.7%, respectively. In addition, our liquidity position is supported by a credit facility with the Federal Home Loan Bank of San Francisco. As of June 30, 2001, we had remaining available borrowing capacity under this credit facility of \$36.0 million, net of the \$1.9 million of additional Federal Home Loan Bank Stock that we would be required to purchase to support those additional borrowings, and \$30.0 million of unused federal funds credit facilities under established lines of credit with two banks.

19

20

CAPITAL RESOURCES

As of June 30, 2001, the Bank's Leverage (Core), Tier I and Total Risk-Based capital ratios were 10.5%, 11.3% and 12.6%, respectively. These ratios were 9.1%, 10.4% and 11.6%, respectively, as of December 31, 2000. The increase in capital ratios from December 31, 2000 to June 30, 2001 was due primarily to the \$14.5 million capital contribution to the Bank from ITLA Capital and the Bank's net income of \$8.4 million, which was partially offset by the payment of \$9.6 million of dividends to ITLA Capital from the Bank. The minimum regulatory requirement for Leverage (Core), Tier I and Total Risk-Based capital are 4.0%, 4.0% and 8.0%, respectively. As of June 30, 2001, the Bank's capital position was designated as "well capitalized" for regulatory purposes.

At June 30, 2001, shareholders equity totaled \$133.8 million or 9.4 percent of total assets. The Company continued to repurchase shares of its common stock in the open market during the second quarter of 2001 completing its fifth stock repurchase program. During the second quarter of 2001, the Company repurchased 422,000 shares of common stock at an average price of \$17.51 per share. For the six months ending June 30, 2001, the Company repurchased 512,000 shares of common stock at an average price of \$17.90 per share. Since beginning share repurchases in April of 1997, the Company has repurchased a total of 1,775,519 shares or approximately 22 percent of the outstanding shares of common stock, returning approximately \$27.9 million of capital to its shareholders at an average price of \$15.71 per share. Through our fifth stock repurchase

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program, 100 percent of the Company's secondary public offering, which raised \$22.6 million in April of 1996 has been retired. The Company's book value per share of common stock was \$21.74 per share as of June 30, 2001, as compared to \$20.05 per share as of December 31, 2000 and \$18.45 per share as of June 30, 2000.

ITEM 3: MARKET RISK

Our estimated sensitivity to interest rate risk, as measured by the estimated interest earnings sensitivity profile and the interest sensitivity gap analysis, has not materially changed from the information disclosed in our annual report on Form 10-K for the year ended December 31, 2000.

20

21

PART II - OTHER INFORMATION

ITEM 1 LEGAL PROCEEDINGS

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

ITEM 2 CHANGES IN SECURITIES

Not applicable.

ITEM 3 DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4 SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

ITEM 5 OTHER INFORMATION

None.

ITEM 6 EXHIBITS AND REPORTS ON FORM 8-K

None

21

22

SIGNATURES

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

ITLA CAPITAL CORPORATION

Date: August 14, 2001

/s/ George W. Haligowski

George W. Haligowski
Chairman of the Board, President and

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Chief Executive Officer

Date: August 14, 2001

/s/ Timothy M. Doyle

Timothy M. Doyle
Managing Director and Chief
Financial Officer