ITLA CAPITAL CORP
Form 10-K
March 16, 2006

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

FORM 10-K

(Mark One)
[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Fiscal Year Ended December 31, 2005

OR

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

For the Transition Period From __________________ To __________________

Commission File Number 0-26960

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

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

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

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

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes [X] No [ ]

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the

Act. Yes [ ] No [X]

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer" in Rule 12b-2 of the Exchange Act. Large Accelerated Filer [ ] Accelerated Filer [X] Non-Accelerated Filer [ ]

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

As of March 7, 2006, there were issued and outstanding 5,583,295 shares of the Registrant's Common Stock. The aggregate market value of the voting stock held by non-affiliates of the Registrant as of June 30, 2005, computed by reference to the closing price of such stock as of June 30, 2005, was $310.9 million. (The exclusion from such amount of the market value of the shares owned by any person shall not be deemed an admission by the Registrant that such person is an affiliate of the Registrant.)

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ITLA CAPITAL CORPORATION

FORM 10-K

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2005

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Forward-Looking Statements

"Safe Harbor" statement under the Private Securities Litigation Reform Act of 1995: This Form 10-K contains forward-looking statements that are subject to risks and uncertainties, including, but not limited to, changes in economic conditions in our market areas, changes in policies by regulatory agencies, the impact of competitive loan products, loan demand risks, the quality or composition of our loan or investment portfolios, increased costs from pursuing the national expansion of our small balance multi-family lending platform and operational challenges inherent in implementing this expansion strategy, fluctuations in interest rates and changes in the relative differences between short and long-term interest rates, levels of non-performing assets and other loans of concern, and operating results, the economic impact of any terrorist actions on our loan originations and loan repayments and other risks detailed from time to time in our filings with the Securities and Exchange Commission. We caution readers not to place undue reliance on forward-looking statements. We do not undertake and specifically disclaim any obligation to revise any forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date of such statements. These risks could cause our actual results for 2006 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", "us", or the "Company" refer to ITLA Capital Corporation and its consolidated subsidiaries.

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PART I

Item 1. Business

General

ITLA Capital Corporation ("ITLA Capital") is the largest financial services company headquartered in San Diego County, California with consolidated assets of $3.1 billion, consolidated net loans of $2.5 billion, consolidated deposits of $1.7 billion and consolidated shareholders' equity of $204.5 million as of December 31, 2005. We conduct and manage our business principally through our wholly-owned subsidiary, Imperial Capital Bank (the "Bank"), an institution with $3.0 billion in assets, with six retail branches located in California, (Beverly Hills, Costa Mesa, Encino, Glendale, San Diego, and San Francisco), and one branch located in Carson City, Nevada. Additionally, the Bank has 27 loan production offices serving the Western United States, the Southeast region, the Mid-Atlantic region, the Ohio Valley, the Metro New York area and New England. On January 1, 2003, the Bank converted from a California industrial bank to a California-chartered commercial bank, and ITLA Capital became a bank holding company. The Bank has been in business for 31 years. Our branch offices are primarily used for our deposit services and lending business. The Company is primarily engaged in:

- Originating and purchasing real estate loans secured by income producing properties for retention in its loan portfolio;
- Originating entertainment finance loans; and
- Accepting customer deposits through the following products: certificates of deposits, money market, passbook and demand deposit accounts. Our deposit accounts are insured by the Federal Deposit Insurance Corporation ("FDIC") up to the legal limits.

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

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

Lending Activities

General. During 2005, our core lending activities were as follows:

- Originating and purchasing real estate loans, including construction loans, secured by income producing properties; and
- Originating entertainment finance loans.

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

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

At December 31, 2005, we had $2.0 billion of income producing property loans outstanding, representing 83.1% of our total real estate loans, including construction loans, and 80.2% of our gross loan portfolio. Most of our real estate borrowers are business owners, individual investors, investment partnerships or limited liability corporations. The income producing property lending that we engage in typically involves loans to a single borrower and is generally viewed as exposing the lender to a greater risk of loss than one- to four-family residential lending, because repayment of the loan generally is dependent, in large part, on the successful operation of the property securing the loan or the business conducted on the property securing the loan. During 2005, we continued the national expansion of our real estate lending platform, and as of December 31, 2005, we had 20 real estate loan production offices located outside of California. In 2005, we also opened our eastern area headquarters in Times Square in New York City. This office was opened to manage and support our eastern seaboard real estate lending efforts.

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

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

We originate real estate loans through our retail branches and loan production offices. These offices are staffed by a total of 57 loan officers. Loan officers solicit mortgage loan brokers for loan applications that meet our underwriting criteria, and also accept applications directly from borrowers. A majority of the real estate loans funded by us are originated through mortgage loan brokers. Mortgage loan brokers act as intermediaries between us and the property owner in arranging real estate loans and earn a fee based upon the principal amount of each loan funded. Since a large portion of our marketing effort is through our loan officers' contacts with mortgage loan brokers, we do not incur significant expenses for advertising our lending services to the general public.

Income producing property loans are generally made in amounts up to 75% of the appraised value of the property; however, in certain instances, multi-family originations may be made at a loan to value ratio of 80%. Loans are generally made for terms of between ten and 30 years, with amortization periods up to 30 years. Depending on market conditions at the time the loan was originated, certain loan agreements may include prepayment penalties.

The average yield on our real estate loan portfolio was 6.99% in 2005 compared to 7.05% in 2004. Our real estate loan portfolio is primarily composed of adjustable rate mortgages indexed to either six month LIBOR or the Prime Rate with interest rate floors, below which the loan's contractual interest rate may not adjust. Approximately 61.8% of our loan portfolio was comprised of adjustable rate loans at December 31, 2005, and approximately 35.8% of the loan portfolio was comprised of hybrid loans, which, after an initial fixed rate period of three or five years, will convert to an adjustable interest rate for the remaining term of the loan. Our adjustable rate loans generally re-price on a quarterly or semi-annual basis with increases generally limited to maximum adjustments of 2% per year up to 5% for the life of the loan. As of December 31, 2005, approximately $2.3 billion or 92.7% of our adjustable rate loan portfolio contained interest rate floors, below which the loans' contractual interest rate may not adjust. The inability of our loans to adjust downward can contribute to increased income in periods of declining interest rates, and also assists us in our efforts to limit the risks to earnings resulting from changes in interest rates, subject to the risk that borrowers may refinance these loans during periods of declining interest rates. At December 31, 2005, the weighted average floor interest rate of our adjustable rate loan portfolio was 6.13%. At that date, approximately $172.0 million or 7.1% of our adjustable rate loan portfolio was at the floor interest rate. At December 31, 2005, 68.2% of the adjustable rate loans outstanding had a lifetime interest rate cap. The weighted-average lifetime interest rate cap on our adjustable rate loan portfolio was 11.33%. At December 31, 2005, none of the loans in our adjustable rate loan portfolio were at the cap rate.

In 2005, 2004, and 2003, we purchased income producing real estate loans totaling $595.3 million, $136.5 million, and $46.8 million, respectively. In our real estate loan purchases, we generally apply the same underwriting criteria as loans internally originated and reserve the right to reject particular loans from a loan pool being purchased that do not meet our underwriting criteria. Loan production in 2005 consisted of the origination of $525.8 million of commercial real estate loans, $322.8 million of small balance multi-family real estate loans, $68.7 million of entertainment finance loans, $2.4 million of franchise loans, and wholesale loan operations acquired $595.3 million of small balance multi-family and $128.5 million of single-family real estate loans.

Construction Loans. We originate construction loans for income producing properties, as well as for single-family residential tract construction. At December 31, 2005, we had $302.9 million of construction loans outstanding, representing 11.9% of our gross loans receivable. In addition to the lending risks previously discussed, construction loans also present risks associated with the accuracy of the initial estimate of the property's value upon completion compared to its actual value, the timely completion of construction activities for their allotted costs and the time needed to stabilize income properties. These risks can be affected by a variety of factors, including the oversight of the project, localized costs for labor and materials, and the weather.

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Entertainment Finance Loans. We conduct our entertainment finance operations through ICB Entertainment Finance ("ICBEF"), a division of the Bank. Typically, ICBEF lends to independent producers of film and television on a senior secured basis. Typically, collateral documents include a mortgage of copyright, security agreements and assigned sales contracts. Credit decisions are based in part on the creditworthiness and reputation of distributors and sales agents who have contracted to distribute the films. ICBEF provides loans (with a typical term of 12 to 18 months) and letters of credit for the production of motion pictures and television shows or series that have a predictable market worldwide, and therefore, a predictable level of revenue arising from licensing of the distribution rights throughout the world.

ICBEF lends to independent producers of film and television, many of which are located in California. ICBEF also has borrowing clients outside of the United States. Independent producers tend to be those producers that do not have major studio distribution outlets for their product. Large film and television studios generally maintain their own distribution outlets and finance their projects with internally generated financing. In addition to funding production loans against a number of distribution contracts, ICBEF may permit an advance, generally not to exceed 20% of the budget amount, against its valuation of unsold rights. ICBEF uses industry standards in the valuation of unsold rights. ICBEF's lending officers review the quality of the distributors and their contracts, the budget, the producer's track record, the script, the genre, talent elements, the schedule of advances, and valuation of all distribution rights when considering a new lending opportunity. Generally, ICBEF loans require the borrower to provide a completion bond that guarantees the completion of the film or the payoff of the outstanding balance of the loan in the event the film is not completed. After closing, each requested advance is approved by the bonding company on a regular basis to ensure that ICBEF is not advancing ahead of an agreed-upon cash flow schedule. The loan documentation grants ICBEF the right to impose certain penalties on the borrower and exercise certain other rights, including replacing the sales agent, if sales are not consummated within the appropriate time. Loans are repaid principally from revenue received from distribution contracts. In many instances, the distribution contracts provide for multiple payments payable at certain milestones (such as execution of contract, commencement of principal photography or completion of principal photography). The maturity date of the loan is generally six to nine months after completion of the production. Delivery of the completed production is typically made to the various distributors upon or after their minimum guarantees have been paid in full. To the extent a distributor fails to make payment upon completion of the film, or the predicted level of revenue is less than expected, we may incur a loss if rights cannot be resold for the same amount or other loan collateral cannot cover required loan payments.

ICBEF typically charges its customers an interest rate of six month LIBOR plus a margin (exclusive of loan fees) on the outstanding balance of the loan. Loan fees typically range from 1.00% to 2.25% with an additional fee up to 7.00% depending on the unsecured amount of the production budget being financed.

At December 31, 2005 and 2004, our entertainment finance portfolio totaled $66.5 million and $99.7 million, respectively, representing 2.6% and 5.5% of our gross loan portfolio as of these dates. Of these amounts, approximately $3.6 million and $12.2 million, respectively, were issued to producers domiciled outside of the United States. These foreign loans were primarily issued to producers located in Australia, Canada and Germany. Approximately $7.7 million, $7.0 million and $5.1 million of interest income was earned during 2005, 2004 and 2003, respectively, in connection with these loans.

Franchise Loans. During 2005, we closed our franchise lending operations and sold approximately $110.0 million, or 89.0%, of the remaining loans within this portfolio. The Bank does not currently anticipate originating or purchasing franchise loans in the future. Prior to the closure, we operated our franchise lending operations through a division of the Bank, Imperial Franchise Finance, based in Tempe, Arizona. Franchise loans are loans to owners of businesses, both franchisors and franchisees, such as fast food restaurants or gasoline retailers that are affiliated with nationally or regionally recognized chains and brand names. Various combinations of land, building, business equipment and fixtures may secure these loans, or they may be a general obligation of the borrower based on a valuation of the borrower's business and debt service ability. These loans may be viewed as riskier than our real estate secured loans, as in each case, the primary source of repayment of a franchise loan is the cash flow of the business and not the underlying value of the collateral. In addition, in certain cases, the success of the borrower's business depends on the management talents and efforts of one or two persons or a small group of persons, and the death, disability or resignation of one or more of these persons could have a material adverse impact on the business. Many of these borrowers have smaller market shares than their competition, may be more vulnerable to economic downturns, often need additional capital to expand or compete and may experience substantial variations in operating results, any of which might impair the borrower's ability to repay a loan. As of December 31, 2005 and 2004, our franchise loan portfolio was $13.7 million and $137.5 million, respectively, which represented 0.5% and 7.6%, respectively, of our gross loan portfolio as of those dates.

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Loan Underwriting. Many of our loans are made to lower credit grade borrowers or the property securing the loan has other factors such as debt-to-income ratios or property location that prevent the borrower from obtaining a prime interest rate. We attempt to mitigate the risk associated with these loans by charging higher interest rates and through our loan approval and loan purchasing process. Initial loan review for potential applications is performed by the Regional Directors and Area Manager of our loan production offices, in consultation with the Chief Underwriter, the respective Deputy Chief Credit Officer, and the Vice Chairman/Chief Credit Officer. Our loan underwriters are responsible for detailed reviews of borrowers, collateral, and loan terms, and prepare a written presentation for every loan application submitted to the real estate loan committee, which is comprised of the following Bank officers:

- Chairman, President, and Chief Executive Officer
- Vice Chairman and Chief Credit Officer
- Executive Managing Director/Chief Operating Officer
- Senior Managing Director/Chief Lending Officer
- Senior Managing Director/Chief of Lending Operations
- Managing Director/Business Credit
- First Vice President/Manager Loan Underwriting
- First Vice President/Loan Administration
- First Vice President/Manager and Chief Underwriter - Express Operations

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

All real estate secured loans over $3.0 million must be submitted to the loan committee for approval. At least one loan committee member or designee must personally conduct on-site inspections of any property involved in connection with a real estate loan recommendation of $2.0 million or more. Loans up to $750,000 may be approved by any loan committee member. Loans of $750,000 to $2.0 million require approval by any two members of the Bank's loan committee, while loans in excess of $2.0 million require approval of three loan committee members, one of whom must be the Chief of Lending Operations or the Manager Loan Underwriting, and only one of whom may be from the Loan Production Unit. Additionally, loans over $3.0 million require the additional signature of the Vice Chairman and Chief Credit Officer; and individual loans over $5.0 million, loans resulting in an aggregate borrowing relationship to one borrower in excess of $7.5 million, and all purchased loan pools must be approved by the Executive Committee of the Bank's Board of Directors.

All entertainment finance loans over $1.0 million are submitted to the business lending loan committee for approval. All loans must be approved by the Managing Director/Business Credit and loans over $3.0 million must be approved by the Vice Chairman and Chief Credit Officer. Individual loans over $7.5 million, loans resulting in an aggregate borrowing relationship to one borrower in excess of $10.0 million, and all purchased loan pools must be approved by the executive committee of the Bank's Board of Directors.

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

The maximum size of a single loan made by the Bank is limited by California law to 25% of the Bank's equity capital. At December 31, 2005, that limit was approximately $65.0 million. Our largest combined credit extension to related borrowers was $34.0 million at December 31, 2005. At December 31, 2005, we had a total of 144 extensions of credit, with a combined outstanding principal balance of $608.3 million, that were over $5.0 million to a single borrower or related borrowers. All combined extensions of credit over $5.0 million were performing in accordance with their repayment terms, with the exception of two credit relationships that are nonaccrual loans and have combined outstanding principal balance of $10.1 million and $7.0 million, respectively. At December 31, 2005, we had 2,937 real estate loans outstanding, with an average balance per loan of approximately $837,000.

Servicing and Collections. Our loan portfolio is predominantly serviced by the Bank's loan servicing department, which is designed to provide prompt customer service, and accurate and timely information for account follow-up, financial reporting and management review. We monitor our loans to ensure that projects are performing as underwritten. This monitoring allows us to take a proactive approach to addressing projects that do not perform as planned. When payments are not received by their contractual due date, collection efforts begin on the fifth day of delinquency with a telephone contact, and proceed to written notices that progress from reminders of the borrower's payment obligation to an advice that a notice of default may be forthcoming. Accounts delinquent for more than 30 days are generally transferred to the Bank's asset management department which, following a review of the account and management approval, implements a collection or restructure plan, or a disposition strategy, and evaluates any potential loss exposure on the asset.

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

Imperial Capital Real Estate Investment Trust

During 2000, we acquired all of the equity and certain collateralized mortgage obligations (“CMOs”) of the ICCMAC Multi-family and Commercial Trust 1999-1 (“ICCMAC Trust”) through our real estate investment trust subsidiary, Imperial Capital Real Estate Investment Trust (“Imperial Capital REIT”). During 2004, the CMOs were retired and the ICCMAC Trust was dissolved. The remaining outstanding loans were contributed to the Imperial Capital REIT. At December 31, 2005, the Imperial Capital REIT held net real estate loans of $3.1 million. The cash flow from the Imperial Capital REIT loan pool provides cash flow on a monthly basis to ITLA Capital. ITLA Capital recorded $1.5 million of pre-tax income from its investment in the Imperial Capital REIT during the year ended December 31, 2005.

Non-performing Assets and Other Loans of Concern

At December 31, 2005, non-performing assets totaled $28.2 million or 0.92% of total assets. Non-performing assets consisted of $24.3 million of non-accrual loans and $4.0 million of other real estate owned consisting of two properties. For additional information regarding non-performing assets see “Item 7: Management’s Discussion and Analysis of Financial Condition and Results of Operations-Credit Risk Elements”.

As of December 31, 2005, we had loans with an aggregate outstanding balance of $66.4 million with respect to which known information concerning possible credit problems with the borrowers or the cash flows of the properties securing the respective loans has caused management to be concerned about the ability of the borrowers to comply with present loan repayment terms. This may result in the future inclusion of such loans in the non-accrual loan category. All of these loans are classified as substandard pursuant to the regulatory guidelines discussed below.

Classified Assets

Management uses a loan classification system consistent with the classification system used by bank regulatory agencies to help it evaluate the risks inherent in its real estate loan portfolio. Loans are identified as “pass”, “substandard”, “doubtful” or “loss” based upon consideration of all sources of repayment, underlying collateral values, current and anticipated economic conditions, trends and uncertainties, and historical experience. Pass loans are further divided into four additional sub-categories, based on the borrower’s financial strength and ability to service the debt and/or the value and debt service coverage of the underlying collateral. Underlying collateral values for real estate dependent loans are supported by property appraisals or evaluations. We review our loan classifications on at least a quarterly basis. At December 31, 2005, we classified $80.1 million of loans as “substandard”, $10.5 million as “doubtful” and none as “loss” of which, $24.3 million of these classified loans were included in the non-performing assets table in “Item 7. Management’s Discussion and Analysis of Results of Financial Condition and Operations - Credit Risk Elements”.

Funding Sources

The primary source of funding for our lending operations and investments are deposits. Our deposits are federally insured by the FDIC to the maximum extent permitted by law. Approximately 86.3% of our deposits are term deposits that pay fixed rates of interest for periods ranging from 90 days to five years, 10.7% of our deposits are variable rate passbook accounts and variable rate money market accounts with limited checking features, and 3.0% are customer demand deposit accounts.

In connection with the Bank's charter conversion in 2003, from an industrial bank to a commercial bank, we expanded our line of banking products and services offered to our customers. The new products and services consist of commercial banking products and services, including consumer and business checking accounts. Our retail checking account balance was $51.9 million at December 31, 2005. We generally accumulate deposits by relying on renewals of term accounts by existing depositors, participating in deposit rate surveys which promote the rates offered by us on our deposit products, and periodically advertising in various local market newspapers and other media. Management believes that our deposits are a reliable funding source and that the cost of funds resulting from our deposit gathering strategy is comparable to those of other banks pursuing a similar strategy. However, because we compete for deposits primarily on the basis of rates, we could experience difficulties in attracting deposits if we could not continue to offer deposit rates at levels above those of other financial institutions. Management also believes that any efforts to significantly increase the size of our deposit base may require greater marketing efforts and/or increases in deposit rates. At December 31, 2005, we had $152.7 million of brokered deposits.

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

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The Bank also uses advances from the FHLB of San Francisco and borrowings from other unaffiliated financial institutions as funding sources. FHLB advances are collateralized by pledges of qualifying cash equivalents, investment securities, mortgage-backed securities and loans. At December 31, 2005, FHLB advances outstanding totaled $932.0 million, and the remaining available borrowing capacity, based on the loans and securities pledged as collateral, totaled $241.4 million, net of the $12.7 million of additional FHLB Stock that we would be required to purchase to support the additional borrowings. Additionally, the Bank has a $60.6 million repurchase agreement borrowing from an unaffiliated financial institution that is secured by mortgage-backed securities. The Bank also has uncommitted, unsecured lines of credit with other banks renewable daily in the amount of $80.0 million and ITLA Capital has a $25.0 million revolving credit facility with an unaffiliated financial institution. This revolving credit facility matures on April 30, 2006, which we intend on renewing upon maturity. See "Item 8. Financial Statements and Supplementary Data — Notes to Consolidated Financial Statements — Notes 7, 8, and 9".

Regulation

As a bank holding company, ITLA Capital is regulated by the Board of Governors of the Federal Reserve System (the "Federal Reserve Board" or "FRB"). As a California-chartered commercial bank, the Bank is regulated by the California Department of Financial Institutions (the "DFI") and the Federal Deposit Insurance Corporation (the "FDIC").

Holding Company Regulation

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

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

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

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

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

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

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

Regulatory Capital Requirements. The Federal Reserve has established risk-based measures and a leverage measure of capital adequacy for bank holding companies.

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

The minimum ratio of total capital to risk-weighted assets is 8.0%. Total capital consists of two components, Tier 1 capital and Tier 2 capital. Tier 1 capital generally consists of common shareholders’ equity, including retained earnings, noncumulative perpetual preferred stock, certain trust preferred securities and minority interest in equity accounts of fully consolidated subsidiaries, less goodwill and other specified intangible assets. Tier 1 capital must equal at least 4.0% of risk-weighted assets. Tier 2 capital generally consists of subordinated debt and other hybrid capital instruments, other preferred stock, a limited amount of loan loss reserves and a limited amount of unrealized holding gains on equity securities. The total amount of Tier 2 capital is limited to 100% of Tier 1 capital. At December 31, 2005, our ratio of total capital to risk-weighted assets was 13.0% and our ratio of Tier 1 capital to risk-weighted assets was 11.0%.

In addition, the Federal Reserve has established minimum leverage ratio guidelines for bank holding companies. These guidelines provide for a minimum ratio of Tier 1 capital to average assets, less goodwill and other specified intangible assets, of 3.0% for certain bank holding companies that meet specified criteria, including having the highest regulatory rating and implementing the Federal Reserve’s risk-based capital measure for market risk. All other bank holding companies generally are required to maintain a leverage ratio of at least 4.0%. At December 31, 2005, ITLA Capital’s required leverage ratio was 4.0% and its actual leverage ratio was 9.1%.

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

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

Bank Regulation — California Law

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

Bank Regulation — Federal Law

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

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

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

Tier 1 Capital Ratio. FDIC regulations establish a minimum 3.0% ratio of tier 1 capital to total average assets for the most highly-rated state-chartered, FDIC-supervised banks. All other FDIC supervised banks must maintain at least a 4.0% tier 1 capital ratio. At December 31, 2005, the Bank's required minimum tier 1 capital ratio was 4.0% and its actual tier 1 capital ratio was 9.1%.

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

For purposes of the risk-based capital requirements, "total capital" means tier 1 capital plus supplementary or tier 2 capital, so long as the amount of supplementary or tier 2 capital that is used to satisfy the requirement does not exceed the amount of tier 1 capital. Tier 2 capital includes cumulative and certain other perpetual preferred stock, mandatory convertible subordinated debt and perpetual subordinated debt, mandatory redeemable preferred stock, intermediate-term preferred stock, mandatory convertible subordinated debt and subordinated debt, the allowance for loan losses up to a maximum of 1.25% of risk-weighted assets and a limited amount of unrealized holding gains on securities. At December 31, 2005 the Bank's required minimum tier 1 risk-based and total capital ratios were 4.0% and 8.0% respectively and its actual was 11.0% and 12.2%, respectively.

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

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

An institution is treated as "well capitalized" if its total risk based capital ratio is 10.0% or more, its tier 1 risk-based ratio is 6.0% or more, its tier 1 capital ratio is 5.0% or greater, and it is not subject to any order or directive by the FDIC to meet a specific capital level. The Bank exceeded these requirements at December 31, 2005.

The FDIC is authorized and, under certain circumstances, required to take certain actions against institutions that fail to meet their capital requirements. The FDIC is generally required to take action to restrict the activities of an "undercapitalized" institution. An undercapitalized institution is one that does not meet the FDIC's minimum capital ratio requirements. Any such institution must submit a capital restoration plan and, until such plan is approved by the FDIC, may not increase its assets, acquire another institution, establish a branch or engage in any new activities, and generally may not make capital distributions. The capital restoration plan must include a limited guaranty by the institution's holding company. In addition, the FDIC must appoint a receiver or conservator for an institution, with certain limited exceptions, within 90 days after it becomes "critically undercapitalized".

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

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

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

Privacy Provisions. Banking regulators, as required under the Gramm-Leach-Bliley Act ("GLB Act"), have adopted rules limiting the ability of banks and other financial institutions to disclose nonpublic information about consumers to nonaffiliated third parties. The rules generally require disclosure of privacy policies to consumers and, in some circumstances, allow consumers to prevent disclosure of certain personal information to nonaffiliated third parties. The privacy provisions of the GLB Act affect how consumer information is transmitted through diversified financial services companies and conveyed to outside vendors.

The state of California has adopted The California Financial Information Privacy Act ("CFPA"), which took effect in 2004. The CFPA requires a financial institution to provide specific information to a consumer related to the sharing of that consumer's nonpublic personal information. A consumer may direct the financial institution not to share his or her nonpublic personal information with affiliated or nonaffiliated companies with which a financial institution has contracted to provide financial products and services, and requires permission from the consumer be acquired by a financial institution prior to sharing such information. These provisions are more restrictive than the privacy provisions of the GLB Act.

In December 2003, the U.S. Congress adopted, and President Bush signed, the Fair and Accurate Transactions Act (the "FACT Act"). In 2005, federal courts determined that the provisions of the CFPA limiting shared information with affiliates are preempted by provisions of the GLB Act, the FACT Act and the Fair Credit Reporting Act.

International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001. President Bush signed the USA Patriot Act of 2001 into law in October 2001. This act contains the International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001 (the "IMLAFA"). The IMLAFA substantially broadened existing anti-money laundering legislation and the extraterritorial jurisdiction of the United States, imposes new compliance and due diligence obligations, creates new crimes and penalties, compels the production of documents located both inside and outside the United States, and clarifies the safe harbor from civil liability to customers. The U.S. Treasury Department has issued a number of regulations implementing the USA Patriot Act that apply certain of its requirements to financial institutions such as the Bank. The regulations impose obligations on financial institutions to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing. The increased obligations of financial institutions, including us, to identify their customers, watch for and report suspicious transactions, respond to requests for information by regulatory authorities and law enforcement agencies, and share information with other financial institutions, requires the implementation and maintenance of internal procedures, practices and controls which have increased, and may continue to increase, our costs and may subject us to liability.

Enforcement and compliance-related activity by government agencies has increased. Money laundering and anti-terrorism compliance are among the areas receiving a high level of focus in the present environment.

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

Employees

As of December 31, 2005, we had 253 employees. Management believes that its relations with employees are satisfactory. We are not subject to any collective bargaining agreements.

Segment Reporting

Financial and other information regarding our operating segments is contained in Note 18 to our audited consolidated financial statements included in Item 8 of this report.

Internet Website

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

Item1A. Risk Factors

An investment in our common stock is subject to risks inherent in our business. Before making an investment decision, you should carefully consider the risks and uncertainties described below together with all of the other information included in this report. In addition to the risks and uncertainties described below, other risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially and adversely affect our business, financial condition and results of operations. The value or market price of our common stock could decline due to any of these identified or other risks, and you could lose all or part of your investment.

Fluctuations in interest rates could reduce our profitability and affect the value of our assets.

Like other financial institutions, we are subject to interest rate risk. Our primary source of income is net interest income, which is the difference between interest earned on loans and investments and the interest paid on deposits and borrowings. We expect that we will periodically experience imbalances in the interest rate sensitivities of our assets and liabilities and the relationships of various interest rates to each other. Over any defined period of time, our interest-earning assets may be more sensitive to changes in market interest rates than our interest-bearing liabilities, or vice versa. In addition, the individual market interest rates underlying our loan and deposit products may not change to the same degree over a given time period. In any event, if market interest rates should move contrary to our position, our earnings may be negatively affected. In addition, loan volume and quality and deposit volume and mix can be affected by market interest rates. Changes in levels of market interest rates could materially adversely affect our net interest spread, asset quality, origination volume and overall profitability.

Interest rates have recently been at historically low levels. However, since June 30, 2004, the U.S. Federal Reserve has increased its target for the federal funds rate thirteen times, from 1.00% to 4.25%. While these short-term market interest rates (which we use as a guide to price our deposits) have increased, longer-term market interest rates (which we use as a guide to price our longer-term loans) have not. This "flattening" of the market yield curve has had a negative impact on our interest rate spread and net interest margin to date. If short-term interest rates continue to rise, and if rates on our deposits and borrowings continue to reprice upwards faster than the rates on our long-term loans and investments, we would experience further compression of our interest rate spread and net interest margin, which would have a negative effect on our profitability.

We principally manage interest rate risk by managing our volume and mix of our earning assets and funding liabilities. In a changing interest rate environment, we may not be able to manage this risk effectively. If we are unable to manage interest rate risk effectively, our business, financial condition and results of operations could be materially harmed.

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Changes in the level of interest rates also may negatively affect our ability to originate real estate loans, the value of our assets and our ability to realize gains from the sale of our assets, all of which ultimately affect our earnings.

An increase in loan prepayments may adversely affect our profitability.

Prepayment rates are affected by consumer behavior, conditions in the real estate and other financial markets, general economic conditions and the relative interest rates on our fixed-rate and adjustable-rate mortgage loans and mortgage-backed securities. Changes in prepayment rates are therefore difficult for us to predict.

We recognize our deferred loan origination costs and premiums paid in originating these loans by adjusting our interest income over the contractual life of the individual loans. As prepayments occur, the rate at which net deferred loan origination costs and premiums are expensed accelerates. The effect of the acceleration of deferred costs and premium amortization may be mitigated by prepayment penalties paid by the borrower when the loan is paid in full within a certain period of time which varies between loans. If prepayment occurs after the period of time when the loan is subject to a prepayment penalty, the effect of the acceleration of premium and deferred cost amortization is no longer mitigated.

We may not be able to reinvest prepayments on loans or mortgage-backed securities at rates comparable to the prepaid instrument particularly in period of declining interest rates.

An inadequate allowance for loan losses would reduce our earnings.

We are exposed to the risk that our borrowers will be unable to repay their loans according to their terms and that any collateral securing the payment of their loans will not be sufficient to assure full repayment. Credit losses are inherent in the lending business and could have a material adverse effect on our operating results. Volatility and deterioration in the economy may also increase our risk for credit losses. We evaluate the collectibility of our loan portfolio and provide an allowance for loan losses that we believe is adequate based upon such factors as:

- the risk characteristics of various classifications of loans;
- general portfolio trends relative to asset and portfolio size;
- potential credit and geographic concentrations;
- delinquency trends and nonaccrual levels;
- historical loss and recovery experience and risks associated with changes in economic, social and business conditions;
- the amount and quality of the collateral;
- the views of our regulators; and
- the underwriting standards in effect when the loan is made.

If our evaluation is incorrect and borrower defaults cause losses exceeding our allowance for loan losses, our earnings could be materially and adversely affected. We cannot assure you that our allowance will be adequate to cover loan losses inherent in our portfolio. We may experience losses in our loan portfolio or perceive adverse trends that require us to significantly increase our allowance for loan losses in the future, which would also reduce our earnings. In addition, the Bank’s regulators, as an integral part of their examination process, may require us to make additional provisions for loan losses.

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Our income producing property loans involve higher principal amounts and expose us to a greater risk of loss than one-to-four family residential loans.

At December 31, 2005, we had $2.0 billion of loans secured by income producing properties, both commercial and multi-family residential, representing 83.1% of our total real estate loans and 80.2% of our gross loan portfolio. The income generated from the operation of the property securing the loan is generally considered by us to be the principal source of repayment on this type of loan. The income producing property lending in which we engage typically involves larger loans to a single borrower and is generally viewed as exposing the lender to a greater risk of loss than one-four family residential lending because these loans generally are not fully amortizing over the loan period, but have a balloon payment due at maturity. A borrower's ability to make a balloon payment typically will depend on being able to either refinance the loan or timely sell the underlying property. Income producing property values are also generally subject to greater volatility than residential property values. The liquidation values of income producing properties may be adversely affected by risks generally incident to interests in real property, such as:

- changes or continued weakness in general or local economic conditions;
- changes or continued weakness in specific industry segments;
- declines in real estate values;
- declines in rental, room or occupancy rates in hotels, apartment complexes or commercial properties
- increases in other operating expenses (including energy costs);
- the availability of refinancing at lower interest rates or better loan terms;
- changes in governmental rules, regulations and fiscal policies, including rent control ordinances, environmental legislation and taxation;
- increases in interest rates, real estate and personal property tax rates, and
- other factors beyond the control of the borrower or the lender.

We generally originate and acquire income producing property loans primarily to be held in our portfolio to maturity. Because the resale market for this type of loan is less liquid than the well-established secondary market for residential loans, should we decide to sell our income producing property loans, we may incur losses on any sale.

The unseasoned nature of many of the loans we originated as part of our small balance multi-family real estate loan platform, along with our limited experience in originating these loans nationwide, may lead to additional provisions for loan losses or charge-offs, which would hurt our profits.

The national expansion of our small balance multi-family real estate loan platform has led to an increase in the number of these types of loans in our portfolio. Many of these loans are unseasoned and have not been subjected to unfavorable economic conditions. We have limited experience in originating these types of loans outside the State of California and as a result do not have a significant payment history pattern with which to judge future collectibility. As a result, it is difficult to predict the future performance of this part of our real estate loan portfolio. These loans may have delinquency or charge-off levels above our historical experience, which could adversely affect our profitability.

Our construction loans are based upon estimates of costs and value associated with the complete project. These estimates may be inaccurate.

We originate construction loans for income producing properties, as well as for single family home construction. At December 31, 2005, construction loans totaled $302.9 million, or 11.9% of gross loans receivable. Construction lending involves additional risks because funds are advanced upon the security of the project, which is of uncertain value prior to its completion. There are also risks associated with the timely completion of the construction activities for their allotted costs, as a number of factors can result in delays and cost overruns, and the time needed to stabilize income producing properties or to sell residential tract developments. Because of the uncertainties inherent in estimating construction costs, as well as the market value of the completed project and the effects of governmental regulation of real property, it is relatively difficult to evaluate accurately the total funds required to complete a project and the related loan-to-value ratio. As a result, construction loans often involve the disbursement of substantial funds with repayment dependent, in part, on the success of the ultimate project and the ability of the borrower to sell or lease the property or refinance the indebtedness, rather than the ability of the borrower or guarantor to repay principal and interest. If our appraisal of the value of the completed project proves to be overstated, we may have inadequate security for the repayment of the loan upon completion of construction of the project and may incur a loss.

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Our real estate lending also exposes us to the risk of environmental liabilities.

In the course of our business, we may foreclose and take title to real estate, and could be subject to environmental liabilities with respect to these properties. We may be held liable to a governmental entity or to third persons for property damage, personal injury, investigation and clean-up costs incurred by these parties in connection with environmental contamination, or may be required to investigate or clean up hazardous or toxic substances, or chemical releases at a property. The costs associated with investigation or remediation activities could be substantial. In addition, as the owner or former owner of a contaminated site, we may be subject to common law claims by third parties based on damages and costs resulting from environmental contamination emanating from the property. If we ever become subject to significant environmental liabilities, our business, financial condition and results of operations could be materially and adversely affected.

Repayment of our entertainment finance loans is primarily dependent on revenues from distribution contracts.

Through ICBEF, a division of the Bank, we originate entertainment finance loans to independent producers of film and television on a senior secured basis. Although these loans are typically collateralized by a mortgage of copyright, security agreements and assigned sales contracts, the primary source of repayment is the revenue received by the borrower from the licensing of distribution rights. For this reason, our credit decisions are based in part on the creditworthiness and reputation of distributors and sales agents who have contracted to distribute the films. In many instances, the distribution contracts provide for multiple payments payable at certain milestones (such as execution of contract, commencement of principal photography or completion of principal photography). The maturity date of the loan is generally six to nine months after completion of the production. To the extent a distributor fails to make payment upon completion of the film, or the predicted level of revenue is less than expected, we may incur a loss if rights cannot be resold for the same amount or other loan collateral cannot cover required loan payments.

Negative events in certain geographic areas, particularly California, could adversely affect us.

Although we have significantly increased the geographic diversification of our loan portfolio in the last two years, our real estate loans remain heavily concentrated in the State of California, with approximately 59.2% of our real estate loans as of December 31, 2005 secured by collateral and made to borrowers in that state. In addition, as of that date, approximately 9.0% and 5.6% of our real estate loans were secured by collateral and made to borrowers in the States of Arizona and Texas, respectively. A worsening of economic conditions in California or in any other state in which we have a significant concentration of borrowers could have a material adverse effect on our business, by reducing demand for new financings, limiting the ability of customers to repay existing loans, and impairing the value of our real estate collateral and real estate owned properties. Real estate values are affected by various other factors, including changes in general or regional economic conditions, governmental rules or policies and natural disasters such as earthquakes, tornados and hurricanes.

Our wholesale funding sources may prove insufficient to replace deposits and support our future growth.

We must maintain sufficient funds to respond to the needs of depositors and borrowers. As a part of our liquidity management, we use a number of funding sources in addition to core deposit growth and repayments and maturities of loans and investments. As we continue to grow, we are likely to become more dependent on these sources, which include brokered certificates of deposit, repurchase agreements, federal funds purchased and Federal Home Loan Bank advances. Adverse operating results or changes in industry conditions could lead to an inability to replace these additional funding sources at maturity. Our financial flexibility will be severely constrained if we are unable to maintain our access to funding or if adequate financing is not available to accommodate future growth at acceptable interest rates. Finally, if we are required to rely more heavily on more expensive funding sources to support future growth, our revenues may not increase proportionately to cover our costs. In this case, our profitability would be adversely affected.

Competition with other financial institutions could adversely affect our profitability.

The banking and financial services industry is very competitive. Legal and regulatory developments have made it easier for new and sometimes unregulated competitors to compete with us. Consolidation among financial service providers has resulted in fewer very large national and regional banking and financial institutions holding a large accumulation of assets. These institutions generally have significantly greater resources, a wider geographic presence or greater accessibility. Our competitors sometimes are also able to offer more services, more favorable pricing or greater customer convenience than we do. In addition, our competition has grown from new banks and other financial services providers that target our existing or potential customers. As consolidation continues among large banks, we expect additional institutions to try to exploit our market.

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Technological developments have allowed competitors including some non-depository institutions, to compete more effectively in local markets and have expanded the range of financial products, services and capital available to our target customers. If we are unable to implement, maintain and use such technologies effectively, we may not be able to offer products or achieve cost-efficiencies necessary to compete in our industry. In addition, some of these competitors have fewer regulatory constraints and lower cost structures.

We rely heavily on the proper functioning of our technology.

We rely on our computer systems, and outside servicers providing technology, for much of our business, including recording our assets and liabilities. If our computer systems or outside technology sources fail, are not reliable or there is a breach of security, our ability to maintain accurate financial records may be impaired, which could materially affect our operations and financial condition.

We are dependent upon the services of our management team.

We are dependent upon the ability and experience of a number of our key management personnel who have substantial experience with our operations, the financial services industry and the markets in which we offer our services. It is possible that the loss of the services of one or more of our senior executives or key managers would have an adverse effect on our operations. Our success also depends on our ability to continue to attract, manage and retain other qualified personnel as we grow. We cannot assure you that we will continue to attract or retain such personnel.

Terrorist activities could cause reductions in investor confidence and substantial volatility in real estate and securities markets.

It is impossible to predict the extent to which terrorist activities may occur in the United States or other regions, or their effect on a particular security issue. It is also uncertain what effects any past or future terrorist activities and/or any consequent actions on the part of the United States government and others will have on the United States and world financial markets, local, regional and national economics, and real estate markets across the United States. Among other things, reduced investor confidence could result in substantial volatility in securities markets, a decline in general economic conditions and real estate related investments and an increase in loan defaults. Such unexpected losses and events could materially affect our results of operations.

We are subject to extensive regulation that could restrict our activities and impose financial requirements or limitations on the conduct of our business.

Bank holding companies and California-charted commercial banks operate in a highly regulated environment and are subject to supervision and examination by federal and state regulatory agencies. We are subject to the Bank Holding Company Act of 1956, as amended, and to regulation and supervision by the FRB. Imperial Capital Bank is subject to regulation and supervision by the FDIC, and DFI. The cost of compliance with regulatory requirements may adversely affect our results of operations or financial condition. Federal and state laws and regulations govern numerous matters including: changes in the ownership or control of banks and bank holding companies; maintenance of adequate capital and the financial condition of a financial institution; permissible types, amounts and terms of extensions of credit and investments; permissible non-banking activities; the level of reserves against deposits; and restrictions on dividend payments.

The FDIC and DFI possess cease and desist powers to prevent or remedy unsafe or unsound practices or violations of law by banks subject to their regulation, and the FRB possesses similar powers with respect to bank holding companies. These and other restrictions limit the manner in which we may conduct our business and obtain financing.

Item 1B. Unresolved Staff Comments

None.

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Item 2. Properties

The following sets forth the Company's material facilities as of December 31, 2005.

Locations	Office Uses	Square Footage	Year Current Lease Term Expires
La Jolla, CA	West Coast Corporate Headquarters	18,913	2008
La Jolla, CA	Administrative and Marketing	2,325	2008
Glendale, CA	Loan Administration/Asset Management/Bank Branch	6,257	2006
Glendale, CA	Loan Operations Division/Real Estate Lending	8,932	2008
Glendale, CA	Operations Support	6,342	2006
Costa Mesa, CA	Bank Branch/Real Estate Lending	3,609	2006
San Francisco, CA	Bank Branch/Real Estate Lending	5,005	2007
Beverly Hills, CA	Bank Branch	2,218	2010
Encino, CA	Bank Branch/Real Estate Lending	5,145	2009
San Diego, CA	Bank Branch/Real Estate Lending	3,046	2011
Santa Monica, CA	Loan Operations/Real Estate Lending	11,490	2009
Walnut Creek, CA	Real Estate Lending	2,220	2006
Century City, CA	ICB Entertainment Finance	7,003	2008
New York, NY	East Coast Corporate Headquarters	3,810	2009
Carson City, NV	Bank Branch	3,000	2007
Boston, MA	Real Estate Lending	3,309	2007
Atlanta, GA	Real Estate Lending	3,148	2008
Fairfield, CT	Real Estate Lending	1,992	2007

For additional information regarding our premises, see "Item 8. Financial Statements and Supplementary Data — Notes to Consolidated Financial Statements - Note 5".

In February 2006, we relocated our loan operations/real estate lending offices based in Santa Monica, CA and our Glendale Bank Branch to a new facility in Glendale, CA. The combined space occupied by these divisions is 14,164 square feet with a lease expiration of 2012.

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

Item 3. Legal Proceedings

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

During 2005, the Company paid an arbitration award stemming from a "glass ceiling" employment dispute with a former employee who alleged she was passed over for promotion due to her gender. The cost to the Company after application of insurance proceeds received was approximately $330,000. As part of the arbitration proceedings, sexual harassment allegations were disclosed involving former employees. These allegations were dealt with by the

Company in accordance with Board approved policies and procedures, consistent with industry standards and prudent management practices. The Company believes that this dispute was an isolated incident. No other lawsuits have ever been filed against the Company based on either glass ceiling or sexual harassment grounds.

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

No matter was submitted to a vote of security holders, through the solicitation of proxies or otherwise, during the quarter ended December 31, 2005.

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PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters, and Issuer Purchases of Equity Securities

ITLA Capital's common stock is traded on the NASDAQ National Market system under the symbol "ITLA". As of March 7, 2006, there were 123 holders of record of ITLA Capital's common stock representing an estimated 1,450 beneficial shareholders with a total of 5,583,295 shares outstanding. We have not paid any cash dividends since our holding company reorganization in 1996. As a bank holding company, ITLA Capital's ability to pay dividends may be affected by regulations, including those governing the payment of dividends by the Bank to ITLA Capital, which could be a source of funds for any dividends paid by ITLA Capital, as well as by the policies of the Federal Reserve Board. See "Item 1. Business—Regulation" and Note 16 to our consolidated financial statements included in Item 8 of this report.

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

	Market Price			Average Daily
	High	Low	Close	Closing Price
2005				
4th Quarter	$ 53.55	$ 47.35	$ 48.85	$ 50.53
3rd Quarter	59.30	50.50	52.49	54.30
2nd Quarter	56.95	43.36	53.90	49.62
1st Quarter	58.31	49.37	49.96	53.89
2004				
4th Quarter	$ 58.81	$ 44.14	$ 58.79	$ 51.79
3rd Quarter	46.97	37.73	46.20	41.45
2nd Quarter	50.00	36.70	40.41	42.64
1st Quarter	50.81	44.52	49.23	48.61

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

Quarterly Operations (Unaudited)

	For the Quarters Ended			
	March 31	June 30	September 30	December 31
	(in thousands except per share amounts)			
2005				
Interest income	$ 36,752	$ 41,680	$ 48,830	$ 50,896
Interest expense	15,010	19,551	24,991	26,934
Net interest income before provision for loan losses	21,742	22,129	23,839	23,962
Provision for loan losses	750	1,500	1,500	6,500
Non-interest income	(20)	509	485	5,600

General and administrative expense		11,230		11,069		11,973		11,986
Total real estate owned expense, net		(11)		—		—		204
Provision for income taxes		4,102		4,230		4,583		4,567
Net income		5,651		5,839		6,268		6,305
Basic earnings per share	$	0.97	$	1.01	$	1.09	$	1.11
Diluted earnings per share	$	0.93	$	0.98	$	1.06	$	1.08
2004								
Interest income	$	32,083	$	28,188	$	30,678	$	34,005
Interest expense		9,146		8,819		10,544		12,909
Net interest income before provision for loan losses		22,937		19,369		20,134		21,096
Provision for loan losses		1,400		950		1,100		1,275
Non-interest income		13,394		1,045		(165)		234
General and administrative expense		11,352		10,488		9,881		10,313
Total real estate owned expense, net		1,057		(330)		(29)		14
Provision for income taxes		8,738		3,676		3,519		4,015
Net income		13,784		5,630		5,498		5,713
Basic earnings per share	$	2.21	$	0.91	$	0.91	$	0.98
Diluted earnings per share	$	2.07	$	0.86	$	0.86	$	0.93

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Stock Repurchases

The following table sets forth the repurchases of our common stock for the fiscal quarter ended December 31, 2005.

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs[(1)]
October 1, 2005 to October 31, 2005	—	$ —	—	295,626
November 1, 2005 to November 30, 2005	2,400	52.33	2,400	293,226
December 1, 2005 to December 31, 2005	46,230	50.71	46,230	246,996
Total	48,630	$ 50.79	48,630	246,996

(1) Therepurchases during October, November and December 2005 were made under the tenth and eleventh extensions of our stock repurchase program, which were announced on March 9, 2005 and October 18, 2005, respectively. These extensions authorized the repurchase of an additional 5% of the outstanding shares as of their respective authorization dates. At December 31, 2005, 246,996 shares remained available for repurchase under the eleventh extension.

Item 6. Selected Financial Data

The following condensed consolidated statements of operations and financial condition and selected performance ratios as of December 31, 2005, 2004, 2003, 2002, and 2001 and for the years then ended have been derived from our audited consolidated financial statements. The information below is qualified in its entirety by the detailed information included elsewhere herein and should be read along with "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Item 8. Financial Statement and Supplementary Data."

	As of and for the years ended December 31,				
	2005	2004	2003	2002	2001
	(in thousands except per share amount)				
Condensed Consolidated Statements of Operations					
Total interest income	$ 178,158	$ 124,954	$ 115,977	$ 110,608	$ 123,095
Total interest expense	86,486	41,418	30,867	37,322	63,863
Net interest income before provision for loan losses	91,672	83,536	85,110	73,286	59,232
Provision for loan losses	10,250	4,725	7,760	9,030	4,575
Net interest income after provision for loan losses	81,422	78,811	77,350	64,256	54,657
Non-interest income *(1)*	6,574	14,508	15,240	373	1,059
Non-interest expense:					
Compensation and benefits	21,737	21,444	18,870	13,954	11,778
Occupancy and equipment	7,177	5,924	4,839	3,165	2,968

Other general and administrative expenses	17,344	14,666	13,006	9,913	8,072
Real estate owned expense, net	193	712	1,212	1,323	387
Total non-interest expense	46,451	42,746	37,927	28,355	23,205
Income before provision for income taxes and minority interest in income of subsidiary	41,545	50,573	54,663	36,274	32,511
Minority interest in income of subsidiary *(2)(3)*	—	—	6,083	3,481	2,967
Income before provision for income taxes	41,545	50,573	48,580	32,793	29,544
Provision for income taxes	17,482	19,948	18,946	12,788	11,393
NET INCOME	$ 24,063	$ 30,625	$ 29,634	$ 20,005	$ 18,151
BASIC EARNINGS PER SHARE	$ 4.19	$ 5.04	$ 4.91	$ 3.35	$ 2.82
DILUTED EARNINGS PER SHARE	$ 4.04	$ 4.75	$ 4.55	$ 3.16	$ 2.72
Dividends paid	$ —	$ —	$ —	$ —	$ —

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Condensed Consolidated Statements of Financial Condition					
Cash and cash equivalents	$ 93,747	$ 87,580	$ 178,318	$ 160,848	$ 134,241
Investment securities available for sale, at fair value	92,563	66,845	53,093	54,677	29,411
Investment securities held-to-maturity, at amortized cost	233,880	296,028	—	—	—
Stock in Federal Home Loan Bank	43,802	23,200	17,966	16,934	13,464
Loans, net	2,523,480	1,793,815	1,505,424	1,438,234	1,284,528
Interest receivable	16,287	10,695	8,958	9,158	11,144
Other real estate owned, net	3,960	—	7,048	12,593	13,741
Premises and equipment, net	6,718	6,645	5,766	4,197	2,177
Deferred income taxes	12,717	10,468	11,609	13,822	11,869
Goodwill	3,118	3,118	3,118	3,118	—
Other assets	20,924	19,677	26,915	8,384	7,733
Total Assets	$ 3,051,196	$ 2,318,071	$ 1,818,215	$ 1,721,965	$ 1,508,308
Deposit accounts	$ 1,735,428	$ 1,432,032	$ 1,147,017	$ 1,065,911	$ 953,654
Federal Home Loan Bank advances and other borrowings	992,557	584,224	378,003	407,762	378,933
Account payable and other liabilities	32,130	20,491	19,696	10,006	9,674
Junior subordinated debentures *(3)*	86,600	86,600	86,600	—	—
Guaranteed preferred beneficial interests in the Company's junior subordinated deferrable interest debentures *(3)*	—	—	—	81,595	28,118
Shareholders' equity	204,481	194,724	186,899	156,691	137,929
Total Liabilities and Shareholders' Equity	$ 3,051,196	$ 2,318,071	$ 1,818,215	$ 1,721,965	$ 1,508,308
Book value per share	$ 37.85	$ 35.09	$ 31.30	$ 27.11	$ 23.54

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(1) For 2004 and 2003, includes fee income earned in connection with the tax refund lending program pursuant to our strategic alliance with various subsidiaries of Household International, Inc. ("Household"), a wholly owned subsidiary of HSBC Holdings plc (NYSE-HBC). This program was terminated by Household in 2004 subsequent to the tax filing season.

(2) Represents accrued distributions payable on our trust preferred securities.

(3) As a result of our adoption of Financial Interpretation No. 46 (revised) issued by the Financial Accounting Standards Board effective December 31, 2003, we de-consolidated our trust subsidiaries which issued our trust preferred securities. The effect of this was to recognize investments in our trust subsidiaries in other assets, to report the amount of junior subordinated debentures we issued to these trusts as a liability in our consolidated balance sheets and, beginning on the date of adoption, to recognize the interest expense on the junior subordinated debentures in our consolidated statements of income. Prior to the de-consolidation, we reported our trust preferred securities in the mezzanine section of our balance sheet as "guaranteed preferred beneficial interests in the Company's junior subordinated deferrable interest debentures" and recognized distributions paid to the holders of the trust preferred securities as "minority interest in income of subsidiary" in our consolidated statement of

income. See Note 1 to our consolidated financial statements included in Item 8 of this report for further discussion.

	As of and for the years ended December 31,				
	2005	**2004**	**2003**	**2002**	**2001**
Selected Performance Ratios					
Return on average assets	0.90%	1.47%	1.71%	1.41%	1.32%
Return on average shareholders' equity	12.12%	15.44%	16.88%	13.56%	13.28%
Net interest margin *(1)*	3.43%	4.12%	5.03%	5.30%	4.33%
Average interest earning assets to average interest bearing liabilities	109.32%	127.50%	135.03%	113.94%	113.80%
Efficiency ratio *(2)*	47.28%	43.60%	37.79%	38.50%	38.49%
Total general and administrative expense to average assets	1.73%	2.02%	2.29%	1.90%	1.66%
Average shareholders' equity to average assets	7.39%	9.51%	11.16%	10.36%	9.93%
Nonperforming assets to total assets	0.92%	0.63%	0.86%	1.08%	1.92%
Allowance for loan losses to loans held for investment, net *(3)*	1.71%	1.94%	2.14%	2.31%	2.16%
Allowance for loan loss to nonaccrual loans	180.59%	242.17%	392.26%	555.61%	174.30%
Net charge-offs (recoveries) to average loans held for investment, net	0.09%	0.16%	0.52%	0.36%	0.39%

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

(2) *Efficiency ratio represents non-interest expense divided by non-interest income and net interest income before provision for loan losses.*

(3) *Loans before allowance for loan losses.*

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Item 7. Management's Discussion and Analysis of Financial Condition and Resultsof Operations

Application of Critical Accounting Policies and Accounting Estimates

The accounting and reporting policies followed by us conform, in all material respects, to accounting principles generally accepted in the United States and to general practices within the financial services industry. The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. While we base our estimates on historical experience, current information and other factors deemed to be relevant, actual results could differ from those estimates.

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

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

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

The level of the allowance also reflects management's continuing evaluation of geographic and credit concentrations, specific credit risks, loan loss experience, current loan portfolio quality, present economic, political and regulatory conditions and unidentified losses inherent in the current loan portfolio. While management utilizes its best judgment and information available, the ultimate adequacy of the allowance is dependent upon a variety of factors beyond the Company's control, including the performance of our loan portfolio, the economy, changes in interest rates and the view of the regulatory authorities toward loan classifications.

We test the ALL balance by comparing the balance in the ALL to historical trends and peer information. Our management team then evaluates the result of the procedures performed, including the result of our testing, and concludes on the appropriateness of the balance of the ALL in its entirety. See the section captioned "Allowance for Loan Losses and Nonperforming Assets" elsewhere in this discussion for further details of the risk factors considered by management in estimating the necessary level of the allowance for loan losses.

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

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

On January 1, 2006, the Company adopted SFAS No. 123(R), "Share-Based Payment", which will require that stock-based compensation be recorded in the Company's financial statements based on their fair value. See "Adoption and Pending Adoption of Recent Accounting Pronouncements" for further discussion.

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

Adoption and Pending Adoption of Recent Accounting Pronouncements

On December 16, 2004, the Financial Accounting Standards Board ("FASB") issued SFAS No. 123 (revised 2004), "Share-Based Payment", which is a revision of SFAS No. 123. SFAS No. 123(R) supersedes APB Opinion No. 25. Generally, the approach to accounting for share-based payments in SFAS No. 123(R) is similar to the approach described in SFAS No. 123. However, SFAS No. 123(R) requires share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their grant date fair values (i.e., pro forma disclosure is no longer an alternative to financial statement recognition). SFAS No. 123(R) is effective for the Company beginning January 1, 2006. The Company plans to adopt SFAS No. 123(R) using a modified version of prospective application ("modified prospective application"). Under modified prospective application, as it is applicable to the Company, SFAS No. 123(R) applies to new awards and to awards modified, repurchased, or cancelled after January 1, 2006. Additionally, compensation cost for the portion of awards for which the requisite service has not been rendered (generally referring to non-vested awards) that are outstanding as of January 1, 2006 must be recognized as the remaining requisite service is rendered over periods after the adoption of SFAS No. 123(R). The attribution of compensation cost for those earlier awards will be based on the same method and on the same grant-date fair values previously determined for the pro forma disclosures required for companies that did not adopt the fair value accounting method for stock-based employee compensation.

In March 2005, the Securities and Exchange Commission ("SEC") issued SEC Staff Accounting Bulletin No. 107 ("SAB 107"), which expresses views of the staff regarding the interaction between SFAS No. 123(R) and certain SEC rules and regulations and provides the staff's view regarding the valuation of share-based payment arrangements for public entities.

Based on the unvested stock-based compensation awards outstanding as of December 31, 2005, the Company expects to recognize total pre-tax, compensation cost of approximately $250,000 during 2006, or approximately $62,500 during each quarter of 2006, in accordance with the accounting requirements of SFAS 123(R). All unvested options outstanding as of December 31, 2005 will be fully vested by the end of 2006. Future levels of compensation cost recognized related to stock-based compensation awards may be impacted by new awards and/or modifications, repurchases and cancellations of existing awards before and after the adoption SFAS 123(R).

In March 2005, the FASB issued Interpretation No. 47 ("FIN 47"), "Accounting for Conditional Asset Retirement Obligations," an interpretation of SFAS No. 143, "Accounting for Asset Retirement Obligations." FIN 47 generally applies to long-lived assets and requires a liability to be recognized for a conditional asset retirement obligation if the fair value of that liability can be reasonably estimated. The interpretation is effective no later than the end of fiscal years ending after December 15, 2005. We do not expect the application of FIN 47 to have a material impact on our financial condition or results of operations.

In May 2005, the FASB issued SFAS No. 154, "Accounting Changes and Error Corrections", which is a replacement of APB Opinion No. 20, "Accounting Changes", and SFAS No. 3, 'Reporting Accounting Changes in Interim Financial Statements". SFAS No. 154 applies to all voluntary changes in accounting principle, and changes the requirements for accounting for and reporting of a change in accounting principle. SFAS No. 154 requires retrospective application to prior periods' financial statements of a voluntary change in accounting principle unless it is impracticable. APB Opinion No. 20 previously required that most voluntary changes in accounting principle be recognized by including in net income of the period of the change the cumulative effect of changing to the new accounting principle. SFAS No. 154 will be effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. Management does not expect the adoption of SFAS No. 154 on January 1, 2006 to have a material impact on the Company's consolidated results of operations or financial position.

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In November 2005, the FASB issued FASB Staff Position (FSP) FAS 115-1 and FAS 124-1, “The Meaning of Other-Than Temporary Impairment and Its Application to Certain Investments.” The FSP addresses determining when an investment is considered impaired, whether an impairment is other than temporary, and measuring an impairment loss. The FSP also addresses the accounting subsequent to the recognition of an other-than-temporary impairment and required certain disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. The FSP is effective for reporting periods beginning after December 15, 2005. We are currently evaluating the requirements of the FSP and do not expect the application of the FSP to have a material impact on our financial condition or results of operations.

In December 2005, the FASB issued FSP SOP 94-6-1, “Terms of Loan Products That May Give Rise to a Concentration of Credit Risk.” The FSP expands the reporting requirements under SFAS No. 107, “Disclosures about Fair Value of Financial Instruments,” for loan products that are determined to represent a concentration of credit risk, including contractual features where repayments are less than the repayments for fully amortizing loans of an equivalent term and high loan-to-value ratios. The guidance in this FSP is generally effective for interim and annual periods ending after December 19, 2005. We have adopted this FSP and incorporated the reporting requirements into our December 31, 2005 financial statements.

In December 2003, the Accounting Standards Executive Committee of the AICPA issued Statement of Position No. 03-3 (“SOP 03-3”), “Accounting for Certain Loans or Debt Securities Acquired in a Transfer”, which addresses accounting for differences between the contractual cash flows of certain loans and debt securities and the cash flows expected to be collected when loans or debt securities are acquired in a transfer and those cash flow differences are attributable, at least in part, to credit quality. As such, SOP 03-3 applies to loans and debt securities acquired individually, in pools or as part of a business combination and does not apply to originated loans. The application of SOP 03-3 limits the interest income, including accretion of purchase price discounts that may be recognized for certain loans and debt securities. Additionally, SOP 03-3 does not allow the excess of contractual cash flows over cash flows expected to be collected to be recognized as an adjustment of yield, loss accrual or valuation allowance, such as the allowance for possible loan losses. SOP 03-3 requires that increases in expected cash flows subsequent to the initial investment be recognized prospectively through adjustment of the yield on the loan or debt security over its remaining life. Decreases in expected cash flows should be recognized as impairment. In the case of loans acquired in a business combination where the loans show signs of credit deterioration, SOP 03-3 represents a significant change from current purchase accounting practice whereby the acquiree’s allowance for loan losses is typically added to the acquirer’s allowance for loan losses. SOP 03-3 is effective for loans and debt securities acquired by us beginning January 1, 2005. The adoption of this new standard is not expected to have a material impact on our financial statements.

General

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

The following discussion and analysis is intended to identify the major factors that influenced our financial condition as of December 31, 2005 and 2004 and our results of operations for the years ended December 31, 2005, 2004 and 2003. Our primary business involves the acceptance of customer deposits and the origination and purchase of loans secured by income producing real estate and, to a lesser extent, the origination of entertainment finance loans.

Consolidated net income in 2005 was $24.1 million, or $4.04 per diluted share, compared to $30.6 million, or $4.75 per diluted share in 2004 and $29.6 million, or $4.55 per diluted share in 2003. The decrease in net income in 2005 was primarily due to the absence of interest and fee income earned in connection with the Bank’s tax refund lending

("RAL") program, which terminated at the conclusion of the 2004 tax season. Despite the termination of the RAL program, net interest income before provision for loan losses increased 9.7% to $91.7 million for the year ended December 31, 2005, compared to $83.5 million for the year ended December 31, 2004. This increase was due to the growth in the average balance of our loan portfolio, a decrease in the average balance of low yielding short-term and overnight investments, and an increase in the average balance of higher yielding investment securities held-to-maturity as compared to last year. The decline in the average balance of short-term and overnight investment securities was a result of the termination of the RAL program, which generated a substantial level of liquidity during the quarter ended March 31, 2004. The Bank invested this additional liquidity in short-term and overnight investments, which earned a lower yield than the Bank earns on its current investment portfolio. The increase in interest income was partially offset by additional interest expense incurred due to the growth in the average balance of our interest bearing liabilities as compared to last year, deposits repricing to higher current market interest rates, and the addition of new borrowings at higher current market interest rates. Our earnings were negatively impacted by a $5.5 million increase in provision for loan losses recorded during the year, as well as a $3.7 million increase in non-interest expense. Non-interest expense increased due to our continued investment in the national expansion of our real estate lending platform.

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The increase in net income in 2004 as compared to 2003, was primarily due to an increase in interest income to $125.0 million for 2004 as compared to $116.0 million in 2003, and a decrease in provision for loan losses to $4.7 million for 2004 as compared to $7.8 million for 2003. These changes were partially offset by a $4.5 million increase in interest expense, net of the impact of the adoption of FIN 46 on January 1, 2004, a $4.8 million increase in non-interest expense, and a $1.0 million increase in provision for income taxes.

Total loan production including the unfunded portion of loans was $1.6 billion for the year ended December 31, 2005, as compared to $1.0 billion and $794.8 million, respectively, for the years ended December 31, 2004 and 2003. Loan production in 2005 consisted of the origination of $525.8 million of commercial real estate loans, $322.8 million of small balance multi-family real estate loans, $68.7 million of entertainment finance loans, $2.4 million of franchise loans, and wholesale loan operations acquired $595.3 million of small balance multi-family and $128.5 million of single-family real estate loans.

Our average total assets increased approximately 28.8% during 2005 to $2.7 billion. Average cash and investment securities totaled $432.8 million in 2005 compared to $419.5 million in 2004, an increase of $13.3 million, or 3.2%. Average loans receivable totaled $2.2 billion in 2005 compared to $1.6 billion in 2004, an increase of $633.1 million, or 39.4%. Average interest bearing deposit accounts totaled $1.7 billion in 2005 compared to $1.2 billion in 2004, an increase of $426.1 million, or 34.8%. FHLB advances and other borrowings averaged $707.4 million in 2005, compared to $277.8 million in 2004, an increase of $429.6 million, or 154.6%.

The allowance for loan losses as a percentage of our total loans was 1.7% at December 31, 2005, as compared to 1.9% at December 31, 2004. During the year ended December 31, 2005, we had net charge-offs of $1.9 million, compared to $2.6 million during the same period last year.

At December 31, 2005, shareholders' equity totaled $204.5 million or 6.7 percent of total assets. During 2005, we continued our stock repurchase program with the implementation of our tenth and eleventh extensions of the stock repurchase program. For the year ended December 31, 2005, we repurchased 431,738 shares at an average price of $52.40 per share. Since beginning share repurchases in April 1997 through December 31, 2005, a total of 3.3 million shares have been repurchased, returning approximately $90.0 million of capital to our shareholders at an average price of $27.22 per share. Through our stock repurchase program, all of our contributed capital has been returned to shareholders. ITLA Capital’s book value per share of common stock was $37.85 as of December 31, 2005, an increase of 7.9 percent from $35.09 per share as of December 31, 2004.

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Results of Operations

Net Interest Income

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

	Years Ended December 31,								
	2005			2004			2003		
	Average Balance	Income/ Expense	Yield/ Rate	Average Balance	Income/ Expense	Yield/ Rate	Average Balance	Income/ Expense	Yield/ Rate
	(dollars in thousands)								
Assets									
Cash and investment securities	$ 432,774	$ 18,438	4.26%	$ 419,452	$ 9,291	2.22%	$ 277,832	$ 5,399	1.94%
Real estate loans *(1)*	2,016,691	141,061	6.99%	1,368,384	96,460	7.05%	1,242,875	95,307	7.67%
Franchise loans *(1)*	121,768	9,972	8.19%	125,280	8,608	6.87%	66,101	4,772	7.22%
Entertainment finance loans *(1)*	89,420	7,724	8.64%	96,227	7,040	7.32%	99,104	7,433	7.50%
Commercial and other loans *(1)*	11,382	963	8.46%	16,234	3,555	21.90%	7,732	3,066	39.65%
Total loans receivable	2,239,261	159,720	7.13%	1,606,125	115,663	7.20%	1,415,812	110,578	7.81%
Total interest earning assets	2,672,035	$ 178,158	6.67%	2,025,577	$ 124,954	6.17%	1,693,644	$ 115,977	6.85%
Non-interest earning assets	51,549			94,739			70,226		
Allowance for loan losses	(37,978)			(35,214)			(33,508)		
Total assets	$ 2,685,606			$ 2,085,102			$ 1,730,362		
Liabilities and Shareholders' Equity									
Interest bearing deposit accounts:									
Interest bearing demand accounts	$ 51,684	$ 1,236	2.39%	$ 80,052	$ 1,409	1.76%	$ 12,571	$ 136	1.08%
Money market and passbook accounts	177,213	5,308	3.00%	140,637	2,680	1.91%	162,638	2,551	1.57%

Time certificates	1,421,415	47,263	3.33%	1,003,555	23,827	2.37%	832,873	21,929	2.63%
Total interest bearing deposit accounts	1,650,312	53,807	3.26%	1,224,244	27,916	2.28%	1,008,082	24,616	2.44%
FHLB advances and other borrowings	707,391	25,508	3.61%	277,828	7,343	2.64%	246,186	6,251	2.54%
Junior subordinated debentures	86,600	7,171	8.28%	86,600	6,159	7.11%	—	—	—
Total interest bearing liabilities	2,444,303	$ 86,486	3.54%	1,588,672	$ 41,418	2.61%	1,254,268	$ 30,867	2.46%
Non-interest bearing demand accounts	27,671			8,023			2,973		
Other non-interest bearing liabilities	15,086			290,077			297,549		
Shareholders' equity	198,546			198,330			175,572		
Total liabilities and shareholders' equity	$ 2,685,606			$ 2,085,102			$ 1,730,362		
Net interest spread *(2)*			3.13%			3.56%			4.39%
Net interest income before provisions for loan losses		$ 91,672			$ 83,536			$ 85,110	
Net interest margin *(3)*			3.43%			4.12%			5.03%

(1) Before allowance for loan losses and net of deferred loan fees and costs. Net loan fee accretion of $2.9 million, $1.8 million and $2.4 million was included in net interest income for 2005, 2004 and 2003, respectively.
(2) Average yield on interest earning assets minus average rate paid on interest bearing liabilities.
(3) Net interest income divided by total average interest earning assets.

Our primary source of revenue is net interest income. Our net interest income is affected by (a) the difference between the yields recognized on interest earning assets, including loans and investments, and the interest rates paid on interest bearing liabilities, including deposits and borrowings, which is referred to as "net interest spread", and (b) the relative amounts of interest earning assets and interest bearing liabilities. As of December 31, 2005, 2004 and 2003, our ratio of average interest earning assets to average interest bearing liabilities was 109.3%, 127.5% and 135.0%, respectively.

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

	2005 vs. 2004 Increase (Decrease) Due to:			2004 vs. 2003 Increase (Decrease) Due to:		
	Volume	Rate	Total	Volume	Rate	Total
	(in thousands)					
Interest and fees earned on:						
Loans, net	$ 45,191	$ (1,134)	$ 44,057	$ 16,573	$ (11,488)	$ 5,085
Cash and investment securities	306	8,841	9,147	3,793	99	3,892
Total increase (decrease) in interest income	45,497	7,707	53,204	20,366	(11,389)	8,977
Interest paid on:						
Deposit accounts	11,584	14,307	25,891	5,748	(2,448)	3,300
FHLB advances and other borrowings	14,677	3,488	18,165	1,111	(19)	1,092
Junior subordinated debentures	—	1,012	1,012	6,159	—	6,159
Total increase (decrease) in interest expense	26,261	18,807	45,068	13,018	(2,467)	10,551
Increase (decrease) net interest income	$ 19,236	$ (11,100)	$ 8,136	$ 7,348	$ (8,922)	$ (1,574)

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2005 Compared to 2004

Net interest income before provision for loan losses increased to $91.7 million for the year ended December 31, 2005, compared to $83.5 million for the prior year, an increase of 9.7%. The increase was primarily caused by the growth in the average balance of our loan portfolio, a decrease in the average balance of low yielding short-term and overnight investments, and an increase in the average balance of higher yielding investment securities held-to-maturity as compared to last year. The decline in the average balance of short-term and overnight investment securities was a result of the termination of the RAL program, which generated a substantial level of liquidity during the quarter ended March 31, 2004. The Bank invested this additional liquidity in short-term and overnight investments, which earned a lower yield than the Bank earns on its current investment portfolio. The increase in net interest income was partially offset by additional interest expense incurred due to the growth in the average balance of our interest bearing liabilities as compared to the same period last year, deposits repricing to higher current market interest rates, and the addition of new borrowings at higher current market interest rates.

The average yield on our total loan portfolio was 7.13% in 2005 compared to 7.20% in 2004. The average yield on our real estate loan portfolio was 6.99% in 2005 compared to 7.05% in 2004. Our adjustable rate mortgages are indexed to either six month LIBOR or the Prime Rate with interest rate floors, below which the loan's contractual interest rate may not adjust. Approximately 61.8% of our loan portfolio was comprised of adjustable rate loans at December 31, 2005, and approximately 35.8% of the loan portfolio was comprised of hybrid loans, which, after an initial fixed rate period of three or five years, will convert to an adjustable interest rate for the remaining term of the loan. Our adjustable rate loans generally re-price on a quarterly or semi-annual basis with increases generally limited to maximum adjustments of 2% per year up to 5% for the life of the loan. As of December 31, 2005, approximately $2.3 billion or 92.7% of our adjustable rate loan portfolio contained interest rate floors, below which the loans' contractual interest rate may not adjust. The inability of our loans to adjust downward can contribute to increased income in periods of declining interest rates, and also assists us in our efforts to limit the risks to earnings resulting from changes in interest rates, subject to the risk that borrowers may refinance these loans during periods of declining interest rates. At December 31, 2005, the weighted average floor interest rate of our adjustable rate loan portfolio was 6.13%. At that date, approximately $172.0 million or 7.1% of our adjustable rate loan portfolio was at the floor interest rate. At December 31, 2005, 68.2% of the adjustable rate loans outstanding had a lifetime interest rate cap. The weighted-average lifetime interest rate cap on our adjustable rate loan portfolio was 11.33%. At December 31, 2005, none of the loans in our adjustable rate loan portfolio were at the cap rate.

Interest expense on interest bearing liabilities increased $45.1 million, or 108.8%, to $86.5 million in 2005 compared to $41.4 million in 2004. The increase was primarily due to an increase in interest expense on deposits and FHLB advances and other borrowings. Interest expense from deposit accounts increased $25.9 million, or 92.7%, to $53.8 million in 2005 compared to $27.9 million in 2004 due to the growth in interest bearing deposits during 2005 and the increase in the average rate paid on deposits as a result of higher current market interest rates as compared to the prior year. The average rate paid on deposits was 3.26% in 2005 compared to 2.28% in 2004.

Interest expense on FHLB advances and other borrowings increased $18.2 million, or 247.4%, to $25.5 million in 2005 compared to $7.3 million in 2004. This increase was primarily caused by additional borrowings utilized to finance lending and investment activities during the year. The average balance of FHLB advances and other borrowings increased $429.6 million, or 154.6%, to $707.4 million in 2005 compared to $277.8 million in 2004. The increase was further impacted by an increase in the rate paid on FHLB advances and other borrowings, which was 3.61% in 2005 as compared to 2.64% in 2004.

Provision for Loan Losses

Provision for loan losses increased to $10.3 million in 2005 compared to $4.7 million in 2004. The current period provision for loan losses was recorded to provide reserves adequate to support the known and inherent risk of loss in the loan portfolio, and for specific reserves required at December 31, 2005. The provision increased during the year due to an increase in the Bank's other loans of concern, a 40.3% increase in the Bank's loan portfolio, and the increase in non-performing loans. Non-performing loans totaled $24.3 million and $14.7 million, respectively, at December 31, 2005 and 2004. This increase in non-performing loans was primarily attributable to the migration of three loans to non-performing status during the year. See also "Credit Risk Elements - Allowance for Loan Losses and Nonperforming Assets".

Non-interest Income

Non-interest income decreased $7.9 million to $6.6 million in 2005 compared to $14.5 million in 2004. Non-interest income for the current year consisted primarily of a $4.9 million gain recorded in connection with the sale of franchise loans. During 2004, non-interest income primarily consisted of fee income earned in connection with the Bank's RAL program. During 2004, the Bank earned $9.3 million of net premiums on the sale of RAL loans and $4.6 million of processing and administrative fees. Because the RAL program related to the filing of income tax returns, transaction activity was concentrated during the tax season. This resulted in our earning substantially all of our RAL program income in the first quarter of 2004.

Non-interest Expense

General and Administrative Expense

General and administrative expenses increased to $46.3 million for the year ended December 31, 2005, compared to $42.0 million for the same period last year. The increase in general and administrative expenses was caused by the additional overhead expenses incurred in connection with the national expansion of our loan production platform compared to last year. This increase was primarily the result of a full year of overhead expenses incurred during 2005 for offices that were opened throughout the prior year. The Company's efficiency ratio (defined as general and administrative expenses as percentage of net revenue) was 47.3 percent for the year ended December 31, 2005, compared to 43.6 percent for the same period last year. The variance in our efficiency ratio was primarily due to the decline in net revenue earned as a result of the termination of the RAL program and the continued national expansion of our small balance multi-family lending platform. Full time equivalent associates averaged 244 in 2005 compared to 236 in 2004.

Income Taxes

Provision for income taxes decreased to $17.5 million in 2005 compared to $19.9 million in 2004. The decrease in provision for income taxes was due to the decline in taxable income earned in 2005. The effective tax rate was 42.08% and 39.44%, respectively, for 2005 and 2004. The increase in the effective tax rate was principally due to a reduction in the allowable deduction on tax exempt income earned on loans located in designated redevelopment and enterprise zones.

At December 31, 2005, we had a net deferred tax asset of $12.7 million. The deferred tax asset related primarily to loan loss provisions recognized on our financial statements that have not yet been recognized on our income tax returns. During 2005, we had no deferred tax assets relating to net operating loss carry forward deductions. The deferred tax asset was considered fully realizable. Accordingly, no valuation allowance on the deferred tax asset was established in 2005.

2004 Compared to 2003

Net interest income before provision for loan losses decreased to $83.5 million for the year ended December 31, 2004, compared to $85.1 million for the prior year, a decrease of 1.8%. The decrease was primarily caused by the effect of interest expense from our trust preferred securities as a result of the adoption of FIN 46 at December 31, 2003. The adoption of FIN 46 required that, beginning on January 1, 2004, we record the expense incurred on our junior subordinated debentures related to the trust preferred securities as interest expense in the consolidated statements of income. Prior period financial information has not been restated for the adoption of FIN 46, and as a result, amounts recorded relating to interest payments to the trusts were recorded as minority interest in income of subsidiary for all periods prior to January 1, 2004. Excluding the effect of the adoption of FIN 46, net interest income before provision for loan losses increased by $4.6 million, or 5.4 percent, as compared to 2003. This increase was primarily a result of an increase in the average balance of loans outstanding, reflecting an increase in loan production and a decline in loan prepayment speeds experienced during the year, an increase in the average balance of investments held-to-maturity, partially offset by a general decline in our net interest spread and an increase in the average balance of interest bearing liabilities. The decline in net interest spread primarily resulted from a decline in the yield of our loan portfolio as higher yielding loans were repaid and replaced by new loan production at lower current market interest rates and the addition of new borrowings at higher current market interest rates.

The average yield on our total loan portfolio was 7.20% in 2004 compared to 7.81% in 2003. The average yield on our real estate loan portfolio was 7.05% in 2004 and 7.67% in 2003. Our commercial real estate loan portfolio is primarily composed of adjustable rate mortgages indexed to six month LIBOR with interest rate floors, below which the loan's contractual interest rate may not adjust. Approximately 83.2% of our real estate loan portfolio was comprised of adjustable rate loans at December 31, 2004, and approximately 14.5% of the real estate loan portfolio was comprised of loans, which become adjustable rate loans after an initial fixed rate period of three or five years. As of December 31, 2004, approximately $1.6 billion or 87.3% of our real estate loan portfolio contained interest rate floors, below which the loans' contractual interest rate may not adjust. At December 31, 2004, the weighted average floor interest rate of our real estate loan portfolio was 6.32%. At that date, approximately $784.5 million or 49.2% of our real estate loan portfolio was at the floor interest rate. At December 31, 2004, 76.7% of the variable rate loans outstanding in our real estate loan portfolio had a lifetime interest rate cap. The weighted-average lifetime interest rate cap on this portfolio was 11.25%.

Interest expense on interest bearing liabilities increased $10.6 million, or 34.2%, to $41.4 million in 2004 compared to $30.9 million in 2003. The increase was primarily due to an increase of $6.2 million in interest expense caused by the adoption of FIN 46, discussed above, as well as an increase in interest expense on deposits and FHLB advances and other borrowings. Interest expense from deposit accounts increased $3.3 million, or 13.4%, to $27.9 million in 2004 compared to $24.6 million in 2003 due to the growth in interest bearing deposits during 2004 partially offset by a decline in the average rate paid on deposits as a result of lower current market interest rates as compared to the prior year. The average rate paid on deposits was 2.28% in 2004 compared to 2.44% in 2003.

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Interest expense from the CMOs decreased $1.0 million, or 93.4%, to $71,000 in 2004 as compared to $1.1 million in 2003. The decrease was primarily due to a decline in average balance of CMOs, as a result of the loan prepayment speeds experienced in 2004 related to the loans securing the CMOs. The average balance and average yield on the CMOs was $3.9 million and 1.81%, respectively, in 2004 as compared to $44.8 million and 2.40%, respectively, in 2003.

Interest expense from FHLB advances and other borrowings increased $2.1 million to $7.3 million in 2004 compared to $5.2 million in 2003, due to an increase in the average balance and average rate paid on FHLB advances and other borrowings. The average balance of FHLB advances and other borrowings increased $72.5 million, or 36.0%, to $273.9 million in 2004 compared to $201.4 million in 2003. The average rate paid on FHLB advances and other borrowings was 2.65% in 2004 compared to 2.57% in 2003. We have used our borrowing capacity under our FHLB credit line, as well as our other borrowing facilities to fund loan production and the purchase of investments held-to-maturity.

Provision for Loan Losses

Provision for loan losses decreased to $4.7 million in 2004 compared to $7.8 million in 2003. The provision for loan losses was recorded to provide reserves adequate to support the known and inherent risk of loss in the loan portfolio, and for specific reserves required. The decline in the provision for loan losses in 2004 as compared to 2003 reflects the overall geographic diversification of our real estate loan portfolio and the increase in our small balance multi-family loan portfolio caused by the national expansion of this lending platform. See also “Credit Risk Elements - Allowance for Loan Losses and Nonperforming Assets”.

Non-interest Income

Non-interest income decreased $732,000 to $14.5 million in 2004 compared to $15.2 million in 2003. During 2004 and 2003, non-interest income primarily consisted of fee income earned in connection with the Bank’s RAL program with Household. During 2004, the Bank earned $9.3 million of net premiums on the sale of RAL loans and $4.6 million of processing and administrative fees. RAL income earned during 2003 was $9.0 million of net premiums on the sale of RAL loans and $4.6 million of processing and administrative fees, respectively. Because the RAL program related to the filing of income tax returns, transaction activity was concentrated during the tax season. This resulted in our earning substantially all of our RAL program income in the first quarters of 2004 and 2003. As a result of the termination of the RAL program, we expect non-interest income to be materially less in 2005.

Non-interest Expense

General and Administrative Expense

General and administrative expenses increased to $42.0 million during 2004, compared to $36.7 million in 2003. The increase was attributable to the development and continued national expansion of the small balance multi-family real estate lending platform. During 2004, we opened twenty loan production offices. Our efficiency ratio was 43.6 percent for the year ended December 31, 2004, compared to 37.8 percent for 2003, reflecting the national expansion of our small balance multi-family lending platform. Full time equivalent associates averaged 236 in 2004 compared to 209 in 2003.

Real Estate Owned Expense

Real estate owned expense decreased to $712,000 in 2004 compared to $1.2 million in 2003. The decrease was primarily attributable to a $255,000 decrease in real estate owned expenses, caused by the decline in the average balance of other real estate owned ("OREO") maintained during the year and an increase in gain on sale of OREO, net of $375,000, partially offset by an increase of $130,000 in the provision for losses on OREO. See also "Credit Risk Elements - Allowance for Loan Losses and Nonperforming Assets".

Income Taxes

Provision for income taxes increased to $19.9 million in 2004 compared to $18.9 million in 2003. The increase in provision for income taxes was due to the increase in taxable income earned in 2004. The effective tax rate was 39.44% and 39.00%, respectively, for 2004 and 2003. The effective tax rate differed from the applicable statutory federal tax rate due to state income taxes and the state income tax deduction for tax exempt income on loans located in designated redevelopment and enterprise zones and due to federal income tax credits received from a low income housing tax credit investment.

At December 31, 2004, we had a net deferred tax asset of $10.5 million. The deferred tax asset related primarily to loan loss provisions recognized on our financial statements that have not yet been recognized on our income tax returns. During 2004, we had no deferred tax assets relating to net operating loss carry forward deductions. The deferred tax asset was considered fully realizable. Accordingly, no valuation allowance on the deferred tax asset was established in 2004.

Minority Interest in Income of Subsidiary

Minority interest in income of subsidiary, consisting of accrued distributions payable on our trust preferred securities, was none in 2004 and $6.1 million in 2003. As discussed above, the adoption of FIN 46 required that, beginning January 1, 2004, we record the expense incurred on our junior subordinated debentures as interest expense on the consolidated statement of income. During 2004, we recorded $6.2 million of interest expense related to our junior subordinated debentures. See "Item 8. Financial Statements and Supplementary Data — Notes to Consolidated Financial Statements - Note 8".

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Financial Condition

At December 31, 2005 Compared with December 31, 2004

Total assets increased by $733.1 million, or 31.6%, to $3.1 billion at December 31, 2005 compared to $2.3 billion at December 31, 2004. The increase in total assets was primarily due to a $738.0 million increase in our loan portfolio, a $25.7 million increase in investment securities available-for-sale, and a $20.6 million increase in FHLB stock, partially offset by a $62.1 million decline in investment securities held-to-maturity and an $8.3 million increase in the allowance for loan losses. The increase in the loan portfolio was primarily due to the increased loan production and a decline in loan prepayment speeds experienced during 2005 as compared to 2004. The growth in assets was primarily funded by the increase in deposits of $303.4 million and an increase in FHLB advances and other borrowings of $408.3 million. The increase in shareholders' equity was primarily due to the retention of net income and an $8.7 million increase in contributed capital, which is primarily related to the exercise of stock options, partially offset by treasury stock purchases of $22.6 million.

At December 31, 2004 Compared with December 31, 2003

Total assets increased by $500.0 million, or 27.5%, to $2.3 billion at December 31, 2004 compared to $1.8 billion at December 31, 2003. The increase in total assets was due primarily to a $288.4 million, or 19.2%, increase in our net loan portfolio to $1.8 billion at December 31, 2004 from $1.5 billion at December 31, 2003, and a $296.0 million increase in investments held-to-maturity. This increase was partially offset by a $90.7 million, or 50.9%, decrease in cash and cash equivalents. The increase in the loan portfolio was primarily due to the increased loan production and a decline in loan prepayment speeds experienced during 2004 as compared to 2003. The growth in assets was primarily funded by the increase in deposits of $285.0 million and an increase in FHLB advances and other borrowings of $222.1 million, partially offset by a decrease in CMOs outstanding of $15.9 million. The increase in shareholders' equity was primarily due to the retention of net income, partially offset by the increase in treasury stock purchases of $30.3 million.

Loans Receivable, Net

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

	December 31,				
	2005	2004	2003	2002	2001
	(in thousands)				
Real estate loans	$ 2,154,372	$ 1,387,973	$ 1,196,729	$ 1,189,258	$ 1,191,688
Construction loans	302,932	183,207	129,540	101,422	54,129
Total real estate loans	2,457,304	1,571,180	1,326,269	1,290,680	1,245,817
Entertainment finance loans	66,514	99,729	98,630	119,283	—
Franchise loans	13,705	137,477	102,128	54,672	57,617
Commercial and other loans	7,264	11,931	6,869	4,314	—
	2,544,787	1,820,317	1,533,896	1,468,949	1,303,434
Unamortized premium	14,582	6,346	5,429	7,898	9,773
Deferred loan origination costs (fees), net	7,928	2,635	(500)	(5,604)	(2,029)
	2,567,297	1,829,298	1,538,825	1,471,243	1,311,178
Allowance for loan losses	(43,817)	(35,483)	(33,401)	(33,009)	(26,650)
	$ 2,523,480	$ 1,793,815	$ 1,505,424	$ 1,438,234	$ 1,284,528

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The contractual maturities of our loan portfolio at December 31, 2005 are as follows:

	Less Than One Year	Loans Maturing in Between One and Five Years	Greater Than Five Years	Total
	(dollars in thousands)			
Real estate loans	$ 34,390	$ 209,758	$ 1,910,224	$ 2,154,372
Construction loans	168,786	134,146	—	302,932
Entertainment finance loans	64,673	1,841	—	66,514
Franchise loans	7,217	33	6,455	13,705
Commercial and other loans	5,314	1,950	—	7,264
	$ 280,380	$ 347,728	$ 1,916,679	$ 2,544,787
Loans with fixed interest rates	$ 4,495	$ 21,627	$ 4,970	$ 31,092
Loans with variable interest rates	275,885	326,101	1,911,709	2,513,695
	$ 280,380	$ 347,728	$ 1,916,679	$ 2,544,787
Percentage with variable interest rates	98.4%	93.8%	99.7%	98.8%

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

The following table sets forth certain information regarding the real property collateral securing our real estate loan portfolio as of December 31, 2005.

	Number of Loans	Gross Amount	Percent of Total	Range of Principal Balance Min	Max	Average	Nonaccrual Loans
	(dollars in thousands)						
Income Producing Property Loans:							
Multi-family (5 or more units)	2,188	$ 1,508,292	61.38%	$ 4	$ 9,885	$ 689	$ 3,185
Retail	85	97,268	3.96%	22	10,134	1,144	—
Office	64	101,823	4.14%	21	14,063	1,591	—
Hotel	22	64,906	2.64%	13	10,964	2,950	1,151
Industrial/warehouse	34	41,035	1.67%	88	7,000	1,207	—
Mixed-use	70	65,472	2.66%	14	7,968	935	325
Mobile home parks	52	38,971	1.59%	265	2,206	749	—
Assisted living	4	20,097	0.82%	1,631	7,411	5,024	—
Storage	12	41,239	1.68%	724	6,200	3,437	—
Other	102	62,218	2.53%	1	9,110	610	1,414
Total income producing	2,633	2,041,321	83.07%				6,075
Construction and Land:							
Construction	67	302,932	12.33%	1	17,906	4,521	—
Land	5	9,969	0.41%	367	6,968	1,994	—
Total construction and land	72	312,901	12.74%				—
Single-family mortgages:							
Single-family (1-4 units)	232	103,082	4.19%	7	2,583	444	42
	2,937	$ 2,457,304	100.00%				$ 6,117

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The following table sets forth the location of the collateral for our real estate loan portfolios as of December 31, 2005.

	Number of Loans	Gross Amount (dollars in thousands)		Percent of Total
Southern California:				
Los Angeles County	890	$	698,352	28.42%
San Diego County	66		86,207	3.51%
Riverside County	48		87,971	3.58%
Orange County	51		60,402	2.46%
San Bernardino County	54		39,909	1.62%
All Other Southern California Counties	12		22,345	0.91%
Total Southern California	1,121		995,186	40.50%
Northern California:				
Alameda County	92		77,267	3.14%
San Francisco County	63		70,130	2.85%
Contra Costa County	52		46,939	1.91%
Fresno County	61		39,992	1.63%
Santa Clara County	48		28,653	1.17%
San Mateo County	22		26,651	1.08%
Kern County	40		24,965	1.02%
All Other Northern California Counties	172		145,618	5.93%
Total Northern California	550		460,215	18.73%
Outside California:				
Arizona	223		220,034	8.95%
Texas	137		137,686	5.60%
Nevada	82		75,088	3.06%
Colorado	82		54,869	2.23%
Georgia	46		53,908	2.19%
Florida	59		49,998	2.03%
Oregon	55		38,572	1.57%
Massachusetts	62		33,580	1.37%
Washington	41		32,075	1.31%
New York	55		28,530	1.16%
Connecticut	70		25,163	1.02%
New Jersey	50		24,507	1.00%
Other U.S. States	304		227,893	9.28%
Total Outside California	1,266		1,001,903	40.77%
	2,937	$	2,457,304	100.00%

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

The following table sets forth certain information with respect to our loan originations and purchases. Fundings related to the tax refund lending programs, and premiums paid and discounts taken on loans purchased in the secondary market are not included below.

	As of and for the Years Ended December 31, 2005	2004	2003
	(dollars in thousands)		
Gross real estate loans originated	$ 846,685	$ 721,090	$ 599,885
Gross entertainment finance loans originated	68,687	92,179	90,528
Gross franchise loans originated	2,352	52,145	50,333
Gross commercial and other loans originated	1,863	58,342	41,054
Gross franchise loans purchased	—	—	7,244
Gross real estate loans purchased	723,822	136,452	46,809
Total loan production	$ 1,643,409	$ 1,060,208	$ 835,853
Gross loans at end of period	$ 2,544,787	$ 1,820,317	$ 1,533,896
Gross loans weighted-average portfolio yield	7.13%	7.20%	7.81%
Average size of loans retained in the Company's portfolio	$ 803	$ 919	$ 943

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Investment Securities

At December 31, 2005, our investment securities totaled $326.4 million, or 10.7% of our total assets. Our investment securities, including the mortgage-backed securities portfolio, are managed in accordance with a written investment policy adopted by the Board of Directors. It is our general policy to purchase U.S. Government securities and federal agency obligations and other investment grade securities. At December 31, 2005, our entire mortgage-backed securities portfolio consisted of investment grade securities issued by Fannie Mae. Our investment securities portfolio at December 31, 2005, contained neither securities of any issuer nor tax-exempt securities with an aggregate book value in excess of 10% of stockholders' equity, excluding those issued by the United States Government, or its agencies, or Fannie Mae. See "Item 8. Financial Statements and Supplementary Data-Notes to Consolidated Financial Statements-Note 2".

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

	December 31,					
	2005		2004		2003	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(in thousands)					
Investment securities available-for-sale						
U.S. Government Agency	$ 89,897	$ 88,829	$ 61,637	$ 61,347	$ 47,749	$ 47,621
Residual interest in securitized loans	3,257	3,570	5,055	5,368	5,055	5,368
Equity securities	16	164	25	130	25	104
Total investment securities available-for-sale	$ 93,170	$ 92,563	$ 66,717	$ 66,845	$ 52,829	$ 53,093
Investment securities held-to-maturity						
Mortgage-backed securities	$ 233,880	$ 229,025	$ 296,028	$ 295,226	$ —	$ —

During the first quarter of 2002, we formed a limited liability company to issue $86.3 million of asset-backed notes in a securitization of substantially all of our residential loan portfolio, and we recorded a residual interest of $5.6 million, which represented the present value of future cash flows (spread and fees) that were anticipated to be received over the life of the loans. The residual interest is recorded on the consolidated balance sheets in the "Investment securities available-for-sale, at fair value". The value of the residual interest is subject to substantial credit, prepayment, and interest rate risk on the sold residential loans. In accordance with the provisions of SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities", the residual interest is classified as "available-for-sale" and, as such, recorded at fair value with the resultant changes in fair value recorded as unrealized gain or loss in a separate component of shareholders' equity in "accumulated other comprehensive income or loss", until realized. Fair value is determined on a monthly basis based on a discounted cash flow analysis. These cash flows are projected over the lives of the receivables using prepayment, default, and interest rate assumptions that we believe market participants would use for similar financial instruments.

During 2005 and 2004, we recognized an other than temporary impairment of $250,000 and $1.0 million, respectively, in connection with the residual interest. Impairments that are deemed to be other than temporary are charged to non-interest income. In evaluating impairments as other than temporary we consider credit risk, as well as the magnitude and trend of default rates and prepayment speeds of the underlying residential loans.

At December 31, 2005 and 2004, key assumptions used to estimate the fair value of the residual interest based on projected cash flows, and the sensitivity of the value to immediate adverse changes in those assumptions were as follows:

	December 31, 2005	December 31, 2004
Dollars in thousands		
Fair value of retained interest	**$ 3,570**	**$ 5,368**
Weighted average life (in years) - securities	**0.56**	**0.68**
Weighted average life (in years) - residual interest	**2.92**	**3.61**
Weighted average annual prepayment speed	**40.0%**	**26.5%**
Impact of 10% adverse change	$ (22)	$ (236)
Impact of 25% adverse change	$ (34)	$ (630)
Weighted average annual discount rate	**13.0%**	**15.0%**
Impact of 10% adverse change	$ (117)	$ (243)
Impact of 25% adverse change	$ (284)	$ (588)
Weighted average lifetime credit losses	**14.3%**	**25.0%**
Impact of 10% adverse change	$ (79)	$ (262)
Impact of 25% adverse change	$ (211)	$ (700)

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

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The following table indicates the composition of the investment security portfolio assuming these securities are held-to-maturity based on the final maturity of each investment. Mortgage-backed securities are included in maturity categories based on their stated maturity date. Expected maturities may differ from contractual maturities because issuers may have the right to prepay obligations. Equity securities classified as available-for-sale have no maturity and are included in the due in one year or less column.

	Due in One Year or Less		Due after One Year through Five Years		Due after Five Years through Ten Years		Due after Ten Years	
	Balance	Weighted Average Yield	Balance	Weighted Average Yield	Balance	Weighted Average Yield	Balance	Weighted Average Yield
December 31, 2005								
Investment securities available-for-sale								
U.S. Government Agency	$ 32,937	2.82%	$ 55,892	4.08%	$ —	—	$ —	—
Equity securities	164	—	—	—	—	—	—	—
Residual interest in securitized loans	—	—	3,570	—	—	—	—	—
Total investment securities available-for-sale	$ 33,101		$ 59,462		$ —		$ —	
Investment securities held-to-maturity								
Mortgage-backed securities	$ —	—	$ —	—	$ —	—	$ 233,880	4.15%

Liquidity and Deposit Accounts

Liquidity refers to our ability to maintain cash flow adequate to fund operations and meet obligations and other commitments on a timely basis, including the payment of maturing deposits and the origination or purchase of new loans. We maintain a cash and investment securities portfolio designed to satisfy operating and regulatory liquidity requirements while preserving capital and maximizing yield. As of December 31, 2005 and 2004, the Bank's liquidity ratios were 10.5% and 10.0%, respectively, exceeding the DFI regulatory requirement of 1.5%. In addition, the Bank's liquidity position is supported by a credit facility with the FHLB of San Francisco. As of December 31, 2005, the Bank had remaining available borrowing capacity under this credit facility of $241.4 million, net of the $12.7 million of additional FHLB Stock that we would be required to purchase to support those additional borrowings, and $80.0 million of unused federal funds credit facilities under established lines of credit with three other banks. Additionally, we have a $25.0 million revolving credit facility with an unaffiliated bank that expires on April 30, 2006. We intend on renewing this revolving credit facility when it matures.

Total deposit accounts increased approximately $303.4 million to $1.7 billion at December 31, 2005 from $1.4 billion at December 31, 2004. The increase in deposits in 2005 was primarily related to an increase in time certificate of deposits of $323.1 million and an increase in money market and passbook accounts of $14.4 million, partially offset by a decrease in interest bearing demand deposit accounts of $34.6 million. Brokered deposits totaled $152.7 million and $100.0 million at December 31, 2005 and 2004, respectively. Total deposit accounts increased approximately $285.0 million to $1.4 billion at December 31, 2004 from $1.1 billion at December 31, 2003. In both 2005 and 2004, the funds provided from deposits were used primarily to fund the growth in our loan portfolio. Although we compete for deposits primarily on the basis of rates, based on our historical experience regarding retention of deposits, management believes that a significant portion of deposits will remain with us upon maturity on an ongoing basis.

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

	December 31, 2005	December 31, 2004 (in thousands)	December 31, 2003
Non-interest demand accounts	$ 13,660	$ 13,108	$ 9,074
Interest demand accounts	38,197	72,832	38,518
Money market and passbook accounts	186,453	172,092	156,505
Time certificates under $100,000	763,701	703,493	564,207
Time certificates $100,000 and over	733,417	470,507	378,713
	$ 1,735,428	$ 1,432,032	$ 1,147,017

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The following table sets forth the maturities of certificates of deposit $100,000 and over at December 31, 2005 (in thousands):

Certificates of deposit $100,000 and over:		
Maturing within three months	$	298,420
After three but within six months		167,118
After six but within twelve months		205,556
After twelve months		62,323
	$	733,417

Off-Balance Sheet Arrangements

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

Our off-balance sheet arrangements, which principally include lending commitments, are described below. At December 31, 2005, we also had a residual interest of $3.6 million in a qualified special purpose entity formed in 2002 to issue $86.3 million of asset-backed notes in a securitization of substantially all of our residential loan portfolio, and a $2.6 million equity interest in our deconsolidated trusts through which we have issued trust preferred securities. See Notes 8 and 10 of our consolidated financial statements included in Item 8 of this report.

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

At December 31, 2005, our approved loan origination commitments outstanding totaled $252.5 million. Unfunded commercial lines of credit totaled $0.9 million. These lines of credit are commitments for possible future extension of credit to existing customers. These lines of credit are typically uncollateralized and usually do not contain a specified maturity date.

We apply essentially the same credit policies and standards as we do in the lending process when making these commitments. See Note 13 to the consolidated financial statements included in Item 8 of this report for additional information regarding lending commitments.

Contractual Obligations

The following table shows our contractual obligations by expected payment period, as of December 31, 2005. Further discussion of these commitments is included in Notes 6, 8, 9, and 14 to the consolidated financial statements included in Item 8 of this report.

Contractual Obligations	Total	One Year or Less	After One Through Three Years	After Three Through Five Years	More Than Five Years
			(in thousands)		
Long-term FHLB advances and other borrowings	$ 904,352	$ 161,719	$ 438,269	$ 263,358	$ 41,006
Junior subordinated debentures	86,600	—	—	—	86,600

Operating lease obligations		13,660		3,940		5,690		2,596	1,434
Deposits with stated maturity dates		1,497,118		1,369,067		105,582		22,026	443
Purchase obligations		1,336		1,132		204		—	—
	$	2,503,066	$	1,535,858	$	549,745	$	287,980	$ 129,483

FHLB advances and other borrowings have defined terms and under certain circumstances are callable at the option of the lender. The junior subordinated debentures are callable by us under the circumstances and at the times described in Note 8 to the consolidated financial statements included in Item 8 of this report.

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

Purchase obligations represent our contractual service and other operating and marketing obligations.

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Capital Resources

ITLA Capital, the Bank's holding company, had Tier 1 leverage, Tier 1 risk based and total risk-based capital ratios at December 31, 2005 of 9.1%, 11.0%, 13.0%, respectively, which, in the case of the Tier 1 risk-based and total risk-based capital ratios, represents $122.4 million and $72.2 million, respectively, of capital in excess of the amount required to be "well capitalized" for bank holding company regulatory purposes. These ratios were 12.3%, 13.7% and 16.0%, respectively, as of December 31, 2004. Portions of our trust preferred securities presently qualify as Tier 1 and total risk-based capital. See Note 8 to our consolidated financial statements included in Item 8 of this report.

The Bank had Tier 1 leverage, Tier 1 risk based and total risk-based capital ratios at December 31, 2005 of 9.1%, 11.0% and _12.2%, respectively, which represents $119.8 million, $120.3 million and $53.8 million, respectively, of capital in excess of the amount required for the Bank to be "well capitalized" for regulatory purposes. These ratios were 11.0%, 12.2% and 13.5%, respectively, as of December 31, 2004.

Shareholders' equity increased to $204.5 million at December 31, 2005 from $194.7 million at December 31, 2004. The change was primarily due to the increase in retained earnings as a result of $24.1 million of net income earned during the year and an $8.7_ million increase in contributed capital, which is primarily related to the exercise of employee stock options, partially offset by the purchase of $22.6 million of our common stock currently held as treasury stock. There were no dividends declared or paid by us during 2005.

Credit Risk Elements

Allowance for Loan Losses and Nonperforming Assets

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

	As of and for the Years Ended December 31,				
	2005	2004	2003	2002	2001
			(dollars in thousands)		
Balance at beginning of year	$ 35,483	$ 33,401	$ 33,009	$ 26,650	$ 27,186
Provision for loan losses	10,250	4,725	7,760	9,030	4,575
Additions due to acquisitions	—	—	—	2,048	—
Charge offs:					
Real estate loans	(1,584)	(189)	(5,286)	(4,730)	(2,845)
Construction loans	—	—	—	—	(2,419)
Entertainment finance loans	(395)	(2,180)	(800)	—	—
Franchise loans	(451)	—	(661)	—	—
Commercial and other loans	—	(1,121)	(700)	—	—
Total charge-offs	(2,430)	(3,490)	(7,447)	(4,730)	(5,264)
Recoveries:					
Real estate loans	88	89	14	11	153
Entertainment finance loans	426	—	—	—	—
Commercial and other loans	—	758	65	—	—
Total recoveries	514	847	79	11	153
Net charge-offs	(1,916)	(2,643)	(7,368)	(4,719)	(5,111)
Balance at end of the year	$ 43,817	$ 35,483	$ 33,401	$ 33,009	$ 26,650
	$ 2,239,261	$ 1,606,125	$ 1,415,812	$ 1,305,902	$ 1,295,097

Average loans outstanding during the year					
Loans, net, at end of the year *(1)*	$ 2,567,297	$ 1,829,298	$ 1,538,825	$ 1,471,243	$ 1,311,178
Selected Ratios:					
Net charge-offs to average loans outstanding	0.09%	0.16%	0.52%	0.36%	0.39%
Net charge-offs to loans, net *(1)*	0.07%	0.14%	0.48%	0.32%	0.39%
Allowance for loan losses to loans, net *(1)*	1.71%	1.94%	2.14%	2.31%	2.16%
Allowance for loan losses to nonaccrual loans	180.59%	242.17%	392.26%	555.61%	174.30%

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

The allowance for loan losses increased to $43.8 million or 1.71% of our total loan portfolio at December 31, 2005 from $35.5 million or 1.94% of our total loan portfolio at December 31, 2004. The increase in the allowance was due primarily to the provision for loan losses of $10.3 million, less net charge-offs of $1.9 million. The current period provision for loan losses was recorded to provide reserves adequate to support the known and inherent risk of loss in the loan portfolio, and for specific reserves required as of December 31, 2005. The increase in the provision for loan losses in 2005 as compared to 2004 was primarily caused by the growth in our loan portfolio and the increase in non-performing and other loans of concern during the year. During 2005, our loan portfolio increased $738.0 million, non-performing loans increased $9.6 million, and other loans of concern increased $29.3 million. Other loans of concern consist of performing loans which have known information that have caused management to be concerned about the borrowers ability to comply with present loan repayment terms. The decrease in the percentage of the allowance for loan losses to the total loan portfolio primarily reflects the decline in our overall risk profile due to a broader geographic diversification of our real estate loan portfolio resulting from a higher concentration of non-California small balance multi-family loans as a percentage of our total loan portfolio.

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The allowance for loan losses increased to $35.5 million or 1.94% of our total loan portfolio at December 31, 2004 from $33.4 million or 2.14% of our total loan portfolio at December 31, 2003. The increase in the allowance was due primarily to the growth in our loan portfolio, which increased $290.5 million in 2004 as compared to 2003. During 2004, we decreased our provision to $4.7 million compared to $7.8 million in 2003. The 2004 provision for loan losses was recorded to provide reserves adequate to support the known and inherent risk of loss in the loan portfolio, and for specific reserves required as of December 31, 2004. The decline in the provision for loan losses in 2004 as compared to 2003 reflects the enhanced overall geographic diversification of our real estate loan portfolio and the increase in our small balance multi-family loan portfolio caused by the national expansion of this lending platform.

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

	December 31, 2005		2004		2003		2002		2001	
Loan Category:	**Allowance for loan losses**	**% of loans(1)**	**Allowance for loan losses**	**% of loans(1)**	**Allowance for loan losses**	**% of loans(1)**	**Allowance for loan losses**	**% of loans (1)**	**Allowance for loan losses**	**% of loans (1)**
Secured by real estate	$ 34,222	96%	$ 23,543	86%	$ 25,522	87%	$ 28,348	88%	$ 26,650	96%
Entertainment finance	6,770	3%	7,828	5%	4,354	6%	2,961	8%	—	—
Franchise	2,685	1%	4,032	8%	3,185	7%	1,490	4%	—	4%
Commercial and other	140	—	80	1%	340	—	210	—	—	—
Total	$ 43,817	100%	$ 35,483	100%	$ 33,401	100%	$ 33,009	100%	$ 26,650	100%

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

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

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

- the risk characteristics of various classifications of loans;
- general portfolio trends relative to asset and portfolio size;
- asset categories;
- potential credit and geographic concentrations;
- delinquency trends and nonaccrual loan levels;

- historical loss experience and risks associated with changes in economic, social and business conditions; and
- the underwriting standards in effect when the loan was made.

Accordingly, the calculation of the adequacy of the allowance for loan losses is not based solely on the level of nonperforming assets. The quantitative factors, included above, are utilized by our management to identify two different risk groups (1) individual loans (loans with specifically identifiable risks); and (2) homogeneous loans (groups of loan with similar characteristics). We base the allocation for individual loans primarily on risk rating grades assigned to each of these loans as a result of our loan management and review processes. We then assign each risk-rating grade a loss ratio, which is determined based on the experience of management and our independent loan review process. We estimate losses on impaired loans based on estimated cash flows discounted at the loan's original effective interest rate or based on the underlying collateral value. Based on management's experience, we also assign loss ratios to groups of loans. These loss ratios are assigned to the various homogenous categories of the portfolio.

The qualitative factors, included above, are generally utilized to identify other risks inherent in the portfolio and to determine whether the estimated credit losses associated with the current portfolio might differ from historical loss trends. We estimate a range of exposure for each qualitative factor and evaluate the current condition and trend of each factor. Based on this evaluation, we assign a positive, negative or neutral grade to each factor to determine whether the portion of the qualitative reserve is in the high, middle or low end of the range for each factor. Because of the subjective nature of these factors and the judgments required to determine the estimated ranges, the actual losses incurred can vary significantly from the estimated amounts.

Management believes that our allowance for loan losses as of December 31, 2005 was adequate to absorb the known and inherent risks of loss in the loan portfolio at that date. While management believes the estimates and assumptions used in its determination of the adequacy of the allowance are reasonable, there can be no assurance that such estimates and assumptions will not be proven incorrect in the future, or that the actual amount of future provisions will not exceed the amount of past provisions or that any increased provisions that may be required will not adversely impact our financial condition and results of operations. In addition, the determination of the amount of the Bank's allowance for loan losses is subject to review by bank regulators, as part of the routine examination process, which may result in the establishment of additional reserves based upon their judgment of information available to them at the time of their examination.

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

	December 31,					
	2005		2004		2003	
	Amount	Percent of Gross Portfolio	Amount	Percent of Gross Portfolio	Amount	Percent of Gross Portfolio
	(dollars in thousands)					
Period of Delinquency						
30 - 59 days	$ 5,060	0.20%	$ 16,684	0.92%	$ 21,455	1.39%
60 - 89 days	3,678	0.14%	6,018	0.33%	882	0.06%
90 days or more	22,533	0.89%	9,401	0.52%	8,515	0.55%
Total loans delinquent	$ 31,271	1.23%	$ 32,103	1.77%	$ 30,852	2.00%

The decrease in total delinquent loans in 2005 was due primarily to a decrease of $9.8 million of past due commercial real estate loans, partially offset by a $6.7 million increase in past due franchise loans.

We have established a policy that all loans greater than $2.5 million are reviewed annually. This review usually involves obtaining updated information about the collateral and source of repayment. In addition, independent outside consultants periodically review the Bank's loan portfolio and report findings to management and the audit committee of the Board of Directors. Loans considered to warrant special attention are presented to the review and reserve committee, which meets at least monthly to review the status of classified loans, consider new classifications or declassifications, determine the need for and amount of any charge offs, and recommend to our executive committee of the Board of Directors the level of allowance for loan losses to be maintained. If management believes that the collection of the full amount of principal is unlikely and the value of the collateral securing the obligation is insufficient, the difference between the loan balance and the fair market value of the collateral are recognized by a partial charge-off of the loan balance to the collateral's fair value. While real property collateral is held for sale, it is subject to periodic evaluation and/or appraisal. If an evaluation or appraisal indicates that the property will ultimately sell for less than our recorded value plus costs of disposition, the loss is recognized by a charge to allowance for other real estate owned losses.

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

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

	December 31, 2005	2004	2003	2002	2001
	(dollars in thousands)				
Nonaccrual loans:*(1)*					
Real estate	$ 6,117	$ 7,057	$ 4,686	$ 3,913	$ 13,690
Construction	—	—	—	—	1,600
Franchise	7,366	3,874	799	1,986	—
Entertainment finance	10,780	3,721	3,030	—	—
Total nonaccrual loans	24,263	14,652	8,515	5,899	15,290
Other real estate owned, net	3,960	—	7,048	12,593	13,741
Total nonperforming assets	28,223	14,652	15,563	18,492	29,031
Accruing loans past-due 90 days or more with respect to principal or interest	—	—	—	—	—
Performing troubled debt restructurings	10,758	3,096	4,709	7,858	3,752
	$ 38,981	$ 17,748	$ 20,272	$ 26,350	$ 32,783
Nonaccrual loans to total gross loans	0.95%	0.80%	0.55%	0.36%	1.17%
Allowance for loan losses to nonaccrual loans	180.59%	242.17%	392.26%	555.61%	174.30%
Nonperforming assets to total assets	0.92%	0.63%	0.86%	1.08%	1.92%

(1) Includes six loans with a net book balance of $8.5 million that were nonperforming troubled debt restructurings in 2005, four loans with a net book balance of $5.7 million that were nonperforming troubled debt restructurings in 2004, and three loans with a net book balance of $3.8 million that were nonperforming troubled debt restructurings in 2003.

Gross interest income that would have been recorded on nonaccrual loans had they been current in accordance with original terms was $1.6 million and $784,000 for the years ended December 31, 2005 and 2004, respectively. The amount of interest income on such nonaccrual loans included in net income for the years ended December 31, 2005 and 2004 was $340,000 and $63,000, respectively. For the years ended December 31, 2005 and 2004, $1.9 million and $1.1 million, respectively, of gross interest income would have been recorded had the restructured loans been current in accordance with their original terms compared to $1.4 million and $734,000, respectively, of interest income that was included in net income for the same periods.

In 2005, $4.0 million of new other real estate owned was acquired, and $70,000 of other real estate owned was sold, resulting in $4.0 million of other real estate owned at December 31, 2005.

As of December 31, 2005, we had loans with an aggregate outstanding balance of $66.4 million with respect to which known information concerning possible credit problems with the borrowers or the cash flows of the properties securing the respective loans has caused management to be concerned about the ability of the borrowers to comply with present loan repayment terms, which may result in the future inclusion of such loans in the non-accrual loan category. The increase during 2005 in this category of loans was primarily due to the migration of three commercial real estate loans to other loans of concern.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

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

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

In evaluating our exposure to changes in interest rates, certain risks inherent in the method of analysis presented in the following tables must be considered. For example, although certain assets and liabilities may have similar maturities or periods to repricing, they may react in different degrees and at different times to changes in market rates. Additionally, loan prepayments and early withdrawals of time certificates could cause interest sensitivities to vary from those that appear in the following table. Further, certain assets, such as variable rate real estate loans, have features that restrict changes in interest rates on a short-term basis and over the life of the asset. The majority of our variable rate real estate loans may not adjust downward below their initial rate, with increases generally limited to maximum adjustments of 2% per year and up to 5% over the life of the loan. These loans may also be subject to prepayment penalties. At December 31, 2005, 7.1% of our adjustable rate loan portfolio would not adjust downward below the floor rate with the weighted-average minimum interest rate on this portfolio being 9.35% and 68.2% of the total loans outstanding had a lifetime interest rate cap, with the weighted-average lifetime interest rate cap on this portfolio being 11.33%. The anticipated effects of these various factors are considered by management in implementing interest rate risk management activities.

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

The following table shows our estimated earnings sensitivity profile to immediate, parallel shifts in interest rates as of December 31, 2005:

Changes in Interest rates (Basis Points)	Percentage Change in Net Interest Income (12 Months)
+ 200 Over One Year	2.26%
+ 100 Over One Year	1.96%
- 100 Over One Year	-2.97%
- 200 Over One Year	-3.51%

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Another tool used to identify and manage our interest rate risk profile is the static gap analysis. Interest sensitivity gap analysis measures the difference between the assets and liabilities repricing or maturing within specific time periods. The following table presents an estimate of our static GAP analysis as of December 31, 2005.

	Maturing or Repricing in					
	3 months or less	**After 3 Months But Within 1 year**	**After 1 Year But Within 5 Years**	**After 5 Years**	**Non-Interest Sensitive**	**Total**
	(dollars in thousands)					
Assets						
Loans *(1)*	$ 1,010,338	$ 766,248	$ 731,351	$ 59,360	$ —	$ 2,567,297
Cash and cash equivalents	90,977	—	—	—	2,770	93,747
Investment securities available-for-sale	12,991	23,689	55,883	—	—	92,563
Investment securities held-to-maturity	13,036	34,978	112,518	73,348	—	233,880
Noninterest-earning assets less allowance for loan losses and unearned fees	—	—	—	—	63,709	63,709
Total assets	$ 1,127,342	$ 824,915	$ 899,752	$ 132,708	$ 66,479	$ 3,051,196
Liabilities and Shareholders' Equity						
Time certificates under $100,000	$ 249,269	$ 449,037	$ 65,395	$ —	$ —	$ 763,701
Time certificates $100,000 and more	298,420	372,674	62,323	—	—	733,417
Money market and passbook accounts	186,453	—	—	—	—	186,453
Demand deposit accounts	38,197	—	—	—	13,660	51,857
FHLB advances and other borrowings	107,876	142,048	701,627	41,006	—	992,557
Other liabilities	—	—	—	—	32,130	32,130
Junior subordinated debentures	25,000	30,000	16,600	15,000		86,600
Shareholders' equity	—	—	—	—	204,481	204,481
Total liabilities and shareholders' equity	$ 905,215	$ 993,759	$ 845,945	$ 56,006	$ 250,271	$ 3,051,196
Net repricing assets over (under) repricing liabilities equals interest rate sensitivity GAP	$ 222,127	$ (168,844)	$ 53,807	$ 76,702	$ (183,792)	
Cumulative interest rate sensitivity GAP	$ 222,127	$ 53,283	$ 107,090	$ 183,792	$	