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

FORM 10-Q

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

For the quarterly period ended September 30, 2017

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: 1-14100

IMPAC MORTGAGE HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

Maryland

(State or other jurisdiction of
incorporation or organization)

33-0675505

(I.R.S. Employer
Identification No.)

1950 Jamboree Road, Irvine, California 92612

(Address of principal executive offices)

(949) 475-3600

(Registrant's telephone number, including area code)

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 No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)

Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

There were 20,949,679 shares of common stock outstanding as of November 3, 2017.

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES
FORM 10-Q QUARTERLY REPORT

TABLE OF CONTENTS

	<u>Page</u>
<u>PART I. FINANCIAL INFORMATION</u>	
<u>ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS</u>	
<u>Consolidated Balance Sheets as of September 30, 2017 (unaudited) and December 31, 2016</u>	3
<u>Consolidated Statements of Operations for the Three and Nine Months Ended September 30, 2017</u>	
<u>and 2016 (unaudited)</u>	4
<u>Consolidated Statement of Changes in Stockholders' Equity for the Nine Months Ended</u>	
<u>September 30, 2017 (unaudited)</u>	5
<u>Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2017 and 2016</u>	
<u>(unaudited)</u>	6
<u>Notes to Unaudited Consolidated Financial Statements</u>	7
<u>ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND</u>	
<u>RESULTS OF OPERATIONS</u>	32
<u>Forward-Looking Statements</u>	32
<u>The Mortgage Industry and Discussion of Relevant Fiscal Periods</u>	32
<u>Selected Financial Results</u>	33
<u>Status of Operations</u>	33
<u>Liquidity and Capital Resources</u>	37
<u>Critical Accounting Policies</u>	38
<u>Financial Condition and Results of Operations</u>	39
<u>ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	61
<u>ITEM 4. CONTROLS AND PROCEDURES</u>	63
<u>PART II. OTHER INFORMATION</u>	
<u>ITEM 1. LEGAL PROCEEDINGS</u>	64
<u>ITEM 1A. RISK FACTORS</u>	64
<u>ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS</u>	65
<u>ITEM 3. DEFAULTS UPON SENIOR SECURITIES</u>	65
<u>ITEM 4. MINE SAFETY DISCLOSURES</u>	65
<u>ITEM 5. OTHER INFORMATION</u>	65
<u>ITEM 6. EXHIBITS</u>	66
<u>SIGNATURES</u>	66
<u>CERTIFICATIONS</u>	

PART I. FINANCIAL INFORMATION
ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS
IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(in thousands, except share data)

	September 30, 2017 (Unaudited)	December 31, 2016
ASSETS		
Cash and cash equivalents	\$ 34,815	\$ 40,096
Restricted cash	6,605	5,971
Mortgage loans held-for-sale	572,268	388,422
Finance receivables	60,912	62,937
Mortgage servicing rights	158,950	131,537
Securitized mortgage trust assets	3,769,231	4,033,290
Goodwill	104,938	104,938
Intangible assets, net	22,631	25,778
Deferred tax asset, net	24,420	24,420
Other assets	60,607	46,345
Total assets	<u>\$ 4,815,377</u>	<u>\$ 4,863,734</u>
LIABILITIES		
Warehouse borrowings	\$ 591,583	\$ 420,573
MSR financings	25,133	—
Term financing, net	—	29,910
Convertible notes, net	24,972	24,965
Long-term debt	44,561	47,207
Securitized mortgage trust liabilities	3,751,831	4,017,603
Contingent consideration	5,816	31,072
Other liabilities	62,028	61,364
Total liabilities	<u>4,505,924</u>	<u>4,632,694</u>
Commitments and contingencies (See Note 10)		
STOCKHOLDERS' EQUITY		
Series A-1 junior participating preferred stock, \$0.01 par value; 2,500,000 shares authorized; none issued or outstanding	—	—
Series B 9.375% redeemable preferred stock, \$0.01 par value; liquidation value \$16,640; 2,000,000 shares authorized, 665,592 noncumulative shares issued and outstanding as of September 30, 2017 and December 31, 2016	7	7
Series C 9.125% redeemable preferred stock, \$0.01 par value; liquidation value \$35,127; 5,500,000 shares authorized; 1,405,086 noncumulative shares issued and outstanding as of September 30, 2017 and December 31, 2016	14	14
Common stock, \$0.01 par value; 200,000,000 shares authorized; 20,945,165 and 16,019,983 shares issued and outstanding as of September 30, 2017 and December 31, 2016, respectively	209	160
Additional paid-in capital	1,233,105	1,168,125
Net accumulated deficit:		
Cumulative dividends declared	(822,520)	(822,520)
Retained deficit	(101,362)	(114,746)
Net accumulated deficit	<u>(923,882)</u>	<u>(937,266)</u>
Total stockholders' equity	<u>309,453</u>	<u>231,040</u>
Total liabilities and stockholders' equity	<u>\$ 4,815,377</u>	<u>\$ 4,863,734</u>

See accompanying notes to unaudited consolidated financial statements

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)
(Unaudited)

	For the Three Months Ended		For the Nine Months Ended	
	September 30,		September 30,	
	2017	2016	2017	2016
Revenues:				
Gain on sale of loans, net	\$ 42,476	\$ 113,158	\$ 116,602	\$ 245,849
Real estate services fees, net	1,355	2,678	4,492	6,773
Servicing fees, net	8,492	3,789	23,575	8,680
Loss on mortgage servicing rights, net	(10,513)	(15,857)	(18,159)	(41,249)
Other	266	225	541	453
Total revenues	<u>42,076</u>	<u>103,993</u>	<u>127,051</u>	<u>220,506</u>
Expenses:				
Personnel expense	23,062	38,467	69,353	93,025
Business promotion	10,403	10,350	30,744	30,828
General, administrative and other	8,497	7,736	24,845	23,742
Accretion of contingent consideration	396	1,591	1,948	5,244
Change in fair value of contingent consideration	(4,798)	23,215	(11,052)	34,569
Total expenses	<u>37,560</u>	<u>81,359</u>	<u>115,838</u>	<u>187,408</u>
Operating income	4,516	22,634	11,213	33,098
Other income (expense):				
Interest income	57,854	64,932	180,011	201,561
Interest expense	(56,308)	(63,628)	(176,921)	(199,525)
Loss on extinguishment of debt	—	—	(1,265)	—
Change in fair value of long-term debt	104	(8,641)	(2,657)	(7,286)
Change in fair value of net trust assets, including trust REO gains (losses)	(1,745)	1,071	6,578	2,609
Total other income (expense)	<u>(95)</u>	<u>(6,266)</u>	<u>5,746</u>	<u>(2,641)</u>
Earnings before income taxes	4,421	16,368	16,959	30,457
Income tax expense (benefit)	2,104	(130)	3,575	728
Net earnings	<u>\$ 2,317</u>	<u>\$ 16,498</u>	<u>\$ 13,384</u>	<u>\$ 29,729</u>
Earnings per common share:				
Basic	\$ 0.11	\$ 1.28	\$ 0.71	\$ 2.43
Diluted	0.11	1.18	0.71	2.27

See accompanying notes to unaudited consolidated financial statements

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY
(in thousands, except share amounts)
(Unaudited)

	Preferred Shares Outstanding	Preferred Stock	Common Shares Outstanding	Common Stock	Additional Paid-In Capital	Cumulative Dividends Declared	Retained Deficit	Total Stockholders' Equity
Balance, December 31, 2016	2,070,678	\$ 21	16,019,983	\$ 160	\$ 1,168,125	\$ (822,520)	\$ (114,746)	\$ 231,040
Proceeds and tax benefit from exercise of stock options	—	—	89,537	1	569	—	—	570
Stock based compensation	—	—	—	—	1,972	—	—	1,972
Common stock issuance, net	—	—	4,423,381	44	55,410	—	—	55,454
Trust preferred exchange	—	—	412,264	4	7,029	—	—	7,033
Net earnings	—	—	—	—	—	—	13,384	13,384
Balance, September 30, 2017	<u>2,070,678</u>	<u>\$ 21</u>	<u>20,945,165</u>	<u>\$ 209</u>	<u>\$ 1,233,105</u>	<u>\$ (822,520)</u>	<u>\$ (101,362)</u>	<u>\$ 309,453</u>

See accompanying notes to unaudited consolidated financial statements

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(Unaudited)

	For the Nine Months Ended	
	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net earnings	\$ 13,384	\$ 29,729
Loss on sale of mortgage servicing rights	90	10,610
Change in fair value of mortgage servicing rights	20,038	32,048
Loss on extinguishment of debt	1,265	—
Gain on sale of mortgage loans	(106,070)	(212,696)
Change in fair value of mortgage loans held-for-sale	(8,262)	(19,572)
Change in fair value of derivatives lending, net	(2,167)	(14,618)
Provision for repurchases	192	778
Origination of mortgage loans held-for-sale	(5,457,907)	(9,813,665)
Sale and principal reduction on mortgage loans held-for-sale	5,345,665	9,414,794
(Gains) losses from REO	(8,484)	5,971
Change in fair value of net trust assets, excluding REO	1,906	(10,273)
Change in fair value of long-term debt	2,657	7,286
Accretion of interest income and expense	69,075	96,036
Amortization of intangible and other assets	3,576	3,577
Accretion of contingent consideration	1,948	5,244
Change in fair value of contingent consideration	(11,052)	34,569
Amortization of debt issuance costs and discount on note payable	145	398
Stock-based compensation	1,972	1,647
Impairment of deferred charge	591	815
Excess tax benefit from share based compensation	12	—
Net change in restricted cash	(634)	(6,454)
Net change in other assets	(12,735)	(715)
Net change in other liabilities	1,016	19,402
Net cash used in operating activities	<u>(143,777)</u>	<u>(415,089)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net change in securitized mortgage collateral	507,552	461,063
Proceeds from the sale of mortgage servicing rights	805	5,153
Purchase of mortgage servicing rights	(5,618)	—
Finance receivable advances to customers	(714,221)	(672,885)
Repayments of finance receivables	716,246	630,600
Net change in mortgages held-for-investment	2	45
Purchase of premises and equipment	(463)	(147)
Net principal change on investment securities available-for-sale	—	47
Proceeds from the sale of REO	24,159	32,275
Net cash provided by investing activities	<u>528,462</u>	<u>456,151</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net proceeds from issuance of common stock	55,454	47,605
Repayment of MSR financing	(25,000)	—
Borrowings under MSR financing	50,133	—
Repayment of warehouse borrowings	(5,063,915)	(8,988,778)
Borrowings under warehouse agreements	5,234,925	9,543,273
Repayment of term financing	(30,000)	(715)
Payment of acquisition related contingent consideration	(16,152)	(27,996)
Repayment of securitized mortgage borrowings	(595,291)	(588,390)
Principal payments on capital lease	(249)	(393)
Debt issuance costs	(100)	(100)
Tax payments on stock based compensation awards	(341)	—
Proceeds from exercise of stock options	570	210
Net cash used in financing activities	<u>(389,066)</u>	<u>(14,569)</u>
Net change in cash and cash equivalents	(63)	26,493
Cash and cash equivalents at beginning of period	40,096	32,409
Cash and cash equivalents at end of period	<u>\$ 34,815</u>	<u>\$ 58,902</u>
NON-CASH TRANSACTIONS:		
Transfer of securitized mortgage collateral to real estate owned	\$ 15,367	\$ 32,719
Mortgage servicing rights retained from loan sales and issuance of mortgage backed securities	42,728	91,809
Common stock issued upon long-term debt exchange	7,033	—
Common stock issued upon conversion of debt	—	20,000
Acquisition of equipment purchased through capital leases	—	551

See accompanying notes to unaudited consolidated financial statements

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(dollars in thousands, except share and per share data or as otherwise indicated)

Note 1.—Summary of Business and Financial Statement Presentation

Business Summary

Impac Mortgage Holdings, Inc. (the Company or IMH) is a Maryland corporation incorporated in August 1995 and has the following wholly-owned subsidiaries: Integrated Real Estate Service Corporation (IRES), Impac Mortgage Corp. (IMC), IMH Assets Corp. (IMH Assets) and Impac Funding Corporation (IFC).

The Company's operations include the mortgage lending operations and real estate services conducted by IRES and IMC and the long-term mortgage portfolio (residual interests in securitizations reflected as net trust assets and liabilities in the consolidated balance sheets) conducted by IMH. IMC's mortgage lending operations include the activities of CashCall Mortgage (CCM).

Financial Statement Presentation

The accompanying unaudited consolidated financial statements of IMH and its subsidiaries (as defined above) have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments, consisting of normal recurring adjustments considered necessary for a fair presentation, have been included. Operating results for the nine months ended September 30, 2017 are not necessarily indicative of the results that may be expected for the year ending December 31, 2017. These interim period condensed consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements, which are included in the Company's Annual Report on Form 10-K for the year ended December 31, 2016, filed with the United States Securities and Exchange Commission (SEC).

All significant intercompany balances and transactions have been eliminated in consolidation. In addition, certain amounts in the prior periods' consolidated financial statements have been reclassified to conform to the current period presentation.

Management has made a number of material estimates and assumptions relating to the reporting of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period to prepare these consolidated financial statements in conformity with GAAP. Additionally, other items affected by such estimates and assumptions include the valuation of trust assets and trust liabilities, contingencies, the estimated obligation of repurchase liabilities related to sold loans, the valuation of long-term debt, mortgage servicing rights, mortgage loans held-for-sale and derivative instruments, including interest rate lock commitments (IRLC). Actual results could differ from those estimates and assumptions.

Recent Accounting Pronouncements

In November 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2015-17, "Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes." The amendments in ASU 2015-17 eliminate the current requirement for organizations to present deferred tax liabilities and assets as current and noncurrent in a classified balance sheet. Instead, organizations will be required to classify all deferred tax assets and liabilities as noncurrent. The amendments in this ASU are effective for public business entities for financial statements issued for annual periods beginning after December 15, 2016, and interim periods within those annual periods. The amendments may be applied prospectively to all deferred tax liabilities and assets or retrospectively to all periods presented. The Company adopted this change prospectively on January 1, 2017 and the adoption of this ASU did not have a material impact on the Company's consolidated financial statements.

[Table of Contents](#)

In March 2016, the FASB issued ASU 2016-09, “*Improvements to Employee Share-Based Payment Accounting*.” ASU 2016-09 simplifies several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities and classification on the statement of cash flows. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016. The Company adopted this change prospectively on January 1, 2017 and did not adjust prior periods. The adoption of this ASU did not have a material impact on the Company’s consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, “*Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*.” The update amends the guidance in Accounting Standards Codification 230, *Statement of Cash Flows*, and clarifies how entities should classify certain cash receipts and cash payments on the statement of cash flows with the objective of reducing the existing diversity in practice related to eight specific cash flow issues. The amendments in this update are effective for annual periods beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted. The Company does not expect the adoption of this ASU to have a material impact on its consolidated financial statements.

In May 2017, the FASB issued ASU No. 2017-09, “*Compensation - Stock Compensation (Topic 718): Scope of Modification Accounting*.” The update provides guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. This ASU is effective for annual reporting periods beginning after December 15, 2017. Early adoption is permitted. The Company does not expect the adoption of ASU 2016-09 to have a material impact on its consolidated financial statements.

Note 2.—Mortgage Loans Held-for-Sale

A summary of the unpaid principal balance (UPB) of mortgage loans held-for-sale by type is presented below:

	September 30, 2017	December 31, 2016
Government (1)	\$ 161,479	\$ 146,305
Conventional (2)	218,744	168,581
Other (3)	172,948	62,701
Fair value adjustment (4)	19,097	10,835
Total mortgage loans held for sale	\$ 572,268	\$ 388,422

- (1) Includes all government-insured loans including Federal Housing Administration (FHA), Veterans Affairs (VA) and United States Department of Agriculture (USDA).
- (2) Includes loans eligible for sale to Federal National Mortgage Association (Fannie Mae or FNMA) and Federal Home Loan Mortgage Corporation (Freddie Mac or FHLMC).
- (3) Includes non-qualified mortgages (NonQM) and jumbo loans.
- (4) Changes in fair value are included in gain on sale of loans, net in the accompanying consolidated statements of operations.

[Table of Contents](#)

Gain on mortgage loans held-for-sale (LHFS), included in gain on sale of loans, net in the consolidated statements of operations, is comprised of the following for the three and nine months ended September 30, 2017 and 2016:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2017	2016	2017	2016
Gain on sale of mortgage loans	\$ 56,230	\$ 109,059	\$ 143,752	\$ 252,084
Premium from servicing retained loan sales	17,855	40,890	42,728	91,809
Unrealized gains from derivative financial instruments	1,711	5,836	2,462	14,294
Realized losses from derivative financial instruments	(2,484)	(3,098)	(7,526)	(18,687)
Mark to market (loss) gain on LHFS	(1,336)	5,300	8,262	19,572
Direct origination expenses, net	(27,734)	(44,902)	(72,884)	(112,445)
(Provision) recovery for repurchases	(1,766)	73	(192)	(778)
Total gain on sale of loans, net	<u>\$ 42,476</u>	<u>\$ 113,158</u>	<u>\$ 116,602</u>	<u>\$ 245,849</u>

Note 3.—Mortgage Servicing Rights

The Company retains mortgage servicing rights (MSRs) from its sales and securitization of certain mortgage loans or as a result of purchase transactions. MSRs are reported at fair value based on the income derived from the net projected cash flows associated with the servicing contracts. The Company receives servicing fees, less subservicing costs, on the UPB of the loans. The servicing fees are collected from the monthly payments made by the mortgagors or when the underlying real estate is foreclosed upon and liquidated. The Company may receive other remuneration from rights to various mortgagor-contracted fees, such as late charges, collateral reconveyance charges and nonsufficient fund fees, and the Company is generally entitled to retain the interest earned on funds held pending remittance (or float) related to its collection of mortgagor principal, interest, tax and insurance payments.

The following table summarizes the activity of MSRs for the nine months ended September 30, 2017 and year ended December 31, 2016:

	September 30, 2017	December 31, 2016
Balance at beginning of period	\$ 131,537	\$ 36,425
Additions from servicing retained loan sales	42,728	128,273
Addition from purchases	5,618	—
Reductions from bulk sales (1)	(895)	(8,773)
Changes in fair value (2)	(20,038)	(24,388)
Fair value of MSRs at end of period	<u>\$ 158,950</u>	<u>\$ 131,537</u>

- (1) In the first quarter of 2017, the Company sold all but a small portion of its NonQM MSRs.
(2) Changes in fair value are included within loss on mortgage servicing rights, net in the accompanying consolidated statements of operations.

[Table of Contents](#)

At September 30, 2017 and December 31, 2016, the outstanding principal balance of the mortgage servicing portfolio was comprised of the following:

	September 30, 2017	December 31, 2016
Government insured	\$ 2,519,574	\$ 1,359,569
Conventional (1)	13,181,522	10,815,998
NonQM	1,969	175,955
Total loans serviced	<u>\$ 15,703,065</u>	<u>\$ 12,351,522</u>

(1) As of September 30, 2017, the Conventional servicing rights have been pledged as collateral and subject to acknowledgement agreements as part of the MSR Financings. (See Note 4. — Debt – MSR Financings.)

The table below illustrates hypothetical changes in fair values of MSRs, caused by assumed immediate changes to key assumptions that are used to determine fair value. See Note 6.—Fair Value of Financial Instruments for a description of the key assumptions used to determine the fair value of MSRs.

<u>Mortgage Servicing Rights Sensitivity Analysis</u>	September 30, 2017	December 31, 2016
Fair value of MSRs	\$ 158,950	\$ 131,537
Prepayment Speed:		
Decrease in fair value from 10% adverse change	(3,841)	(4,956)
Decrease in fair value from 20% adverse change	(7,930)	(9,593)
Decrease in fair value from 30% adverse change	(12,167)	(13,940)
Discount Rate:		
Decrease in fair value from 10% adverse change	(5,839)	(4,927)
Decrease in fair value from 20% adverse change	(11,277)	(9,511)
Decrease in fair value from 30% adverse change	(16,350)	(13,786)

Sensitivities are hypothetical changes in fair value and cannot be extrapolated because the relationship of changes in assumptions to changes in fair value may not be linear. Also, the effect of a variation in a particular assumption is calculated without changing any other assumption, whereas a change in one factor may result in changes to another. Accordingly, no assurance can be given that actual results would be consistent with the results of these estimates. As a result, actual future changes in MSR values may differ significantly from those displayed above.

Loss on mortgage servicing rights is comprised of the following for the three and nine months ended September 30, 2017 and 2016:

	For the Three Months Ended		For the Nine Months Ended	
	September 30,		September 30,	
	2017	2016	2017	2016
Change in fair value of mortgage servicing rights	\$ (11,177)	\$ (8,224)	\$ (20,038)	\$ (32,048)
Loss on sale of mortgage servicing rights	(8)	(7,532)	(90)	(10,610)
Realized and unrealized gains (losses) from hedging instruments	672	(101)	1,969	1,409
Loss on mortgage servicing rights, net	<u>\$ (10,513)</u>	<u>\$ (15,857)</u>	<u>\$ (18,159)</u>	<u>\$ (41,249)</u>

Servicing fees, net is comprised of the following for the three and nine months ended September 30, 2017 and 2016:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2017	2016	2017	2016
Contractual servicing fees	\$ 9,978	\$ 4,755	\$ 27,356	\$ 10,981
Late and ancillary fees	117	41	275	115
Subservicing and other costs	(1,603)	(1,007)	(4,056)	(2,416)
Servicing fees, net	<u>\$ 8,492</u>	<u>\$ 3,789</u>	<u>\$ 23,575</u>	<u>\$ 8,680</u>

Loans Eligible for Repurchase from Ginnie Mae (GNMA)

The Company routinely sells loans in GNMA guaranteed mortgage-backed securities (MBS) by pooling eligible loans through a pool custodian and assigning rights to the loans to GNMA. When these GNMA loans are initially pooled and securitized, the Company meets the criteria for sale treatment and derecognizes the loans. The terms of the GNMA MBS program allow, but do not require, the Company to repurchase mortgage loans when the borrower has made no payments for three consecutive months. When the Company has the unconditional right, as servicer, to repurchase GNMA pool loans it has previously sold and are more than 90 days past due, the Company then re-recognizes the loans on its consolidated balance sheets in other assets, at their unpaid principal balances, and records a corresponding liability in other liabilities in the consolidated balance sheets. At September 30, 2017 and December 31, 2016, loans eligible for repurchase from GNMA totaled \$25.5 million and \$9.9 million in UPB, respectively.

The loans eligible for repurchase from GNMA are in the Company's servicing portfolio. The Company monitors the delinquency of the servicing portfolio and directs the subservicer to mitigate losses on delinquent loans.

Note 4.—Debt

Warehouse Borrowings

The Company, through its subsidiaries, enters into Master Repurchase Agreements with lenders providing warehouse facilities. The warehouse facilities are uncommitted facilities used to fund, and are secured by, residential mortgage loans from the time of funding until the time of settlement when sold to the investor. In accordance with the terms of the Master Repurchase Agreements, the Company is required to maintain cash balances with the lender as additional collateral for the borrowings, which are included in restricted cash in the accompanying consolidated balance sheets.

The following table presents certain information on warehouse borrowings and related accrued interest for the periods indicated:

	Maximum Borrowing Capacity	Balance Outstanding At		Maturity Date
		September 30, 2017	December 31, 2016	
Short-term borrowings:				
Repurchase agreement 1	\$ 150,000	\$ 121,330	\$ 106,609	June 15, 2018
Repurchase agreement 2	35,000	33,995	44,761	May 28, 2018
Repurchase agreement 3 (1)	225,000	139,436	125,320	December 22, 2017
Repurchase agreement 4	250,000	140,184	52,067	February 27, 2018
Repurchase agreement 5	100,000	57,951	56,655	March 31, 2018
Repurchase agreement 6	200,000	98,687	35,161	June 28, 2018
Total warehouse borrowings	<u>\$ 960,000</u>	<u>\$ 591,583</u>	<u>\$ 420,573</u>	

(1) As of September 30, 2017 and December 31, 2016, \$60.9 million and \$62.9 million, respectively, are associated with finance receivables made to the Company's warehouse customers.

MSR Financings

On August 17, 2017, IMC (Borrower), entered into a Line of Credit Promissory Note with a lender providing for a revolving line of credit of \$30.0 million (FHLMC Financing). The Borrower is able to borrow up to 55% of the fair market value of FHLMC pledged mortgage servicing rights. The Line of Credit has a term until May 31, 2018 and will automatically renew for subsequent one year periods unless the lender provides the Borrowers 150 days' notice of its intention not to renew. Interest payments are payable monthly and accrue interest at the rate per annum equal to LIBOR plus 4.0% and the balance of the obligation may be prepaid at any time. The obligations under the Line of Credit are secured by FHLMC pledged mortgage servicing rights and is guaranteed by Integrated Real Estate Services, Corp. At September 30, 2017, \$5.0 million was outstanding under the FHLMC Financing.

On February 10, 2017, IMC (Borrower), entered into a Loan and Security Agreement (Agreement) with a lender providing for a revolving loan commitment of \$40.0 million for a period of two years (FNMA Financing). The Borrower is able to borrow up to 55% of the fair market value of FNMA pledged servicing rights. Upon the two year anniversary of the Agreement, any amounts outstanding will automatically be converted into a term loan due and payable in full on the one year anniversary of the conversion date. Interest payments are payable monthly and accrue interest at the rate per annum equal to one-month LIBOR plus 4.0% and the balance of the obligation may be prepaid at any time. The Borrower initially drew down \$35.1 million, and used a portion of the proceeds to pay off the Term Financing (approximately \$30.1 million) originally entered into in June 2015 as discussed below. The Borrower also paid the lender an origination fee of \$100 thousand, which is deferred and amortized over the life of the FNMA Financing. At September 30, 2017, \$20.1 million was outstanding under the FNMA Financing.

Term Financing

In June 2015, the Company and its subsidiaries (IRES, IMC and Impac Warehouse Lending, Inc. (IWL), collectively, the Borrowers) entered into a Loan Agreement with a lender pursuant to which the Creditor provided to the Borrowers a term loan in the aggregate principal amount of \$30.0 million (Term Financing) due and payable on December 19, 2016, which could have been extended to December 18, 2017 at the Creditor's discretion. In June 2016, the maturity of the Term Financing was extended to June 16, 2017 and the Company paid an additional \$100 thousand extension fee, which was deferred and amortized over the life of the Term Financing. Interest on the Term Financing was payable monthly and accrued at a rate of one-month LIBOR plus 8.5% per annum. In February 2017, the proceeds from the FNMA Financing were used to pay off the Term Financing.

Convertible Notes

In January 2016, pursuant to the terms of the \$20.0 million Convertible Promissory Notes issued in April 2013 (the Notes), the Company exercised its option to convert the Notes to common stock. The conversion resulted in the Company issuing an aggregate of 1,839,080 shares of common stock in February 2016, at a conversion price of \$10.875 per share. As a result of the transaction, the Company converted \$20.0 million of debt into equity and paid interest through April 2016. No gain or loss was recorded as a result of the transaction.

In May 2015, the Company issued an additional \$25.0 million Convertible Promissory Notes (2015 Convertible Notes). The 2015 Convertible Notes mature on or before May 9, 2020 and accrue interest at a rate of 7.5% per annum, to be paid quarterly. The Company had approximately \$50 thousand in transaction costs, which were deferred and amortized over the life of the 2015 Convertible Notes.

Noteholders may convert all or a portion of the outstanding principal amount of the 2015 Convertible Notes into shares of the Company's common stock (Conversion Shares) at a rate of \$21.50 per share, subject to adjustment for stock splits and dividends (Conversion Price). The Company has the right to convert the entire outstanding principal of the 2015 Convertible Notes into Conversion Shares at the Conversion Price if the market price per share of the common stock, as measured by the average volume-weighted closing stock price per share of the common stock on the NYSE AMERICAN (or any other U.S. national securities exchange then serving as the principal such exchange on which the shares of common stock are listed), reaches the level of \$30.10 for any twenty (20) trading days in any period of thirty

[Table of Contents](#)

(30) consecutive trading days after the Closing Date. Upon conversion of the 2015 Convertible Notes by the Company, the entire amount of accrued and unpaid interest (and all other amounts owing) under the 2015 Convertible Notes are immediately due and payable. Furthermore, if the conversion of the 2015 Convertible Notes by the Company occurs prior to the third anniversary of the Closing Date, then the entire amount of interest under the 2015 Convertible Notes through the third anniversary is immediately due and payable. To the extent the Company pays any cash dividends on its shares of common stock prior to conversion of the 2015 Convertible Notes, upon conversion of the 2015 Convertible Notes, the Noteholders will also receive such dividends on an as-converted basis of the 2015 Convertible Notes less the amount of interest paid by the Company prior to such dividend.

Unless an event of default has occurred and is continuing, each purchaser of the 2015 Convertible Notes agrees, for the three years after the Closing Date, to vote all Conversion Shares for each of the Company's nominees for election to the Company's board of directors and not to nominate any other candidate for election to the board of directors at any time within such three year period.

Long-term Debt

Trust Preferred Securities

During 2005, the Company formed four wholly-owned trust subsidiaries (Trusts) for the purpose of issuing an aggregate of \$99.2 million of trust preferred securities (Trust Preferred Securities). All proceeds from the sale of the Trust Preferred Securities and the common securities issued by the Trusts were originally invested in \$96.3 million of junior subordinated debentures (debentures), which became the sole assets of the Trusts. The Trusts paid dividends on the Trust Preferred Securities at the same rate as paid by the Company on the debentures held by the Trusts.

During 2008 and 2009, the Company purchased and cancelled \$36.5 million in outstanding Trust Preferred Securities for \$5.5 million. Additionally, during 2009, the Company exchanged an aggregate of \$51.3 million in outstanding Trust Preferred Securities for \$62.0 million in Junior Subordinated Notes. As a result of these transactions, \$8.5 million in Trust Preferred Securities remained outstanding.

On May 5, 2017, the Company agreed to exchange 412,264 shares of its common stock for the remaining Trust Preferred Securities which had an aggregate liquidation amount of \$8.5 million issued by Impac Capital Trust #4. Accrued and unpaid interest on the Trust Preferred Securities was paid in cash in the aggregate amount of approximately \$14 thousand. The interest rate on the Trust Preferred Securities was a variable rate of three-month LIBOR plus 3.75% per annum. At the time of the exchange, the interest rate was 4.92%.

The exchange was based on the carrying value of the trust preferred obligation, which was \$5.6 million at March 31, 2017, and an agreed upon stock price that determined a fixed number of shares to be issued in the exchange. However, because the measurement date of the exchange was the date the common stock was issued when the market price of the common stock was \$17.06, the Company recorded a \$1.3 million loss on extinguishment of debt for the difference in stock price from the agreed upon stock price to the stock price on the issuance date of the common stock.

	<u>September 30,</u> <u>2017</u>	<u>December 31,</u> <u>2016</u>
Trust Preferred Securities	\$ —	\$ 8,500
Common securities	—	263
Fair value adjustment	—	(3,197)
Total Trust Preferred Securities	<u>\$ —</u>	<u>\$ 5,566</u>

Junior Subordinated Notes

The Company carries its Junior Subordinated Notes at estimated fair value as more fully described in Note 6.—*Fair Value of Financial Instruments*. The following table shows the remaining principal balance and fair value of junior subordinated notes issued as of September 30, 2017 and December 31, 2016:

[Table of Contents](#)

	<u>September 30,</u> <u>2017</u>	<u>December 31,</u> <u>2016</u>
Junior Subordinated Notes (1)	\$ 62,000	\$ 62,000
Fair value adjustment	(17,439)	(20,359)
Total Junior Subordinated Notes	\$ 44,561	\$ 41,641

- (1) Stated maturity of March 2034; requires quarterly distributions initially at a fixed rate of 2.00% per annum through March 2014 with increases of 1.00% per year in 2014 through 2017. Starting in 2018, the interest rates become variable at 3-month LIBOR plus 3.75% per annum.

Note 5.—Securitized Mortgage Trusts

Securitized Mortgage Trust Assets

Securitized mortgage trust assets, which are recorded at their estimated fair value (FMV), are comprised of the following at September 30, 2017 and December 31, 2016:

	<u>September 30,</u> <u>2017</u>	<u>December 31,</u> <u>2016</u>
Securitized mortgage collateral	\$ 3,758,140	\$ 4,021,891
REO	11,091	11,399
Total securitized mortgage trust assets	\$ 3,769,231	\$ 4,033,290

Securitized Mortgage Trust Liabilities

Securitized mortgage trust liabilities, which are recorded at their estimated FMV, are comprised of the following at September 30, 2017 and December 31, 2016:

	<u>September 30,</u> <u>2017</u>	<u>December 31,</u> <u>2016</u>
Securitized mortgage borrowings	\$ 3,751,831	\$ 4,017,603

Changes in fair value of net trust assets, including trust REO losses, are comprised of the following for the three and nine months ended September 30, 2017 and 2016:

	<u>For the Three Months Ended</u> <u>September 30,</u>		<u>For the Nine Months Ended</u> <u>September 30,</u>	
	<u>2017</u>	<u>2016</u>	<u>2017</u>	<u>2016</u>
Change in fair value of net trust assets, excluding REO	\$ (4,479)	\$ 2,511	\$ (1,906)	\$ 8,580
Gains (losses) from REO	2,734	(1,440)	8,484	(5,971)
Change in fair value of net trust assets, including trust REO gains (losses)	\$ (1,745)	\$ 1,071	\$ 6,578	\$ 2,609

Note 6.—Fair Value of Financial Instruments

The use of fair value to measure the Company's financial instruments is fundamental to its consolidated financial statements and is a critical accounting estimate because a substantial portion of its assets and liabilities are recorded at estimated fair value.

FASB ASC 825 requires disclosure of the estimated fair value of certain financial instruments and the methods and significant assumptions used to estimate such fair values. The following table presents the estimated fair value of financial instruments included in the consolidated financial statements as of the dates indicated:

[Table of Contents](#)

	September 30, 2017				December 31, 2016			
	Carrying Amount	Estimated Fair Value			Carrying Amount	Estimated Fair Value		
		Level 1	Level 2	Level 3		Level 1	Level 2	Level 3
Assets								
Cash and cash equivalents	\$ 34,815	\$34,815	\$ —	\$ —	\$ 40,096	\$40,096	\$ —	\$ —
Restricted cash	6,605	6,605	—	—	5,971	5,971	—	—
Mortgage loans held-for-sale	572,268	—	572,268	—	388,422	—	388,422	—
Finance receivables	60,912	—	60,912	—	62,937	—	62,937	—
Mortgage servicing rights	158,950	—	—	158,950	131,537	—	—	131,537
Derivative assets, lending, net	12,998	—	983	12,015	11,169	—	—	11,169
Securitized mortgage collateral	3,758,140	—	—	3,758,140	4,021,891	—	—	4,021,891
Liabilities								
Warehouse borrowings	\$ 591,583	\$ —	\$591,583	\$ —	\$ 420,573	\$ —	\$420,573	\$ —
MSR financings	25,133	—	—	25,133	—	—	—	—
Term financing	—	—	—	—	29,910	—	—	29,910
Convertible notes	24,972	—	—	24,972	24,965	—	—	24,965
Contingent consideration	5,816	—	—	5,816	31,072	—	—	31,072
Long-term debt	44,561	—	—	44,561	47,207	—	—	47,207
Securitized mortgage borrowings	3,751,831	—	—	3,751,831	4,017,603	—	—	4,017,603
Derivative liabilities, lending, net	—	—	—	—	336	—	336	—

The fair value amounts above have been estimated by management using available market information and appropriate valuation methodologies. Considerable judgment is required to interpret market data to develop the estimates of fair value in both inactive and orderly markets. Accordingly, the estimates presented are not necessarily indicative of the amounts that could be realized in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

For securitized mortgage collateral and securitized mortgage borrowings, the underlying Alt-A (non-conforming) residential and commercial loans and mortgage-backed securities market have experienced significant declines in market activity, along with a lack of orderly transactions. The Company's methodology to estimate fair value of these assets and liabilities include the use of internal pricing techniques such as the net present value of future expected cash flows (with observable market participant assumptions, where available) discounted at a rate of return based on the Company's estimates of market participant requirements. The significant assumptions utilized in these internal pricing techniques, which are based on the characteristics of the underlying collateral, include estimated credit losses, estimated prepayment speeds and appropriate discount rates.

Refer to Recurring Fair Value Measurements below for a description of the valuation methods used to determine the fair value of investment securities available-for-sale, securitized mortgage collateral and borrowings, derivative assets and liabilities, long-term debt, mortgage servicing rights and mortgage loans held-for-sale.

The carrying amount of cash, cash equivalents and restricted cash approximates fair value.

Finance receivables carrying amounts approximate fair value due to the short-term nature of the assets and do not present unanticipated interest rate or credit concerns.

Warehouse borrowings carrying amounts approximate fair value due to the short-term nature of the liabilities and do not present unanticipated interest rate or credit concerns.

Convertible notes are recorded at amortized cost. The estimated fair value is determined using a discounted cash flow model using estimated market rates.

MSR financings carrying amount approximates fair value as the underlying facility bears interest at a rate that is periodically adjusted based on a market index.

Term financing structured debt had a maturity of less than one year. The term financing was recorded at amortized cost. The carrying amount approximated fair value due to the short-term nature of the liability and did not present unanticipated interest rate or credit concerns.

Fair Value Hierarchy

The application of fair value measurements may be on a recurring or nonrecurring basis depending on the accounting principles applicable to the specific asset or liability or whether management has elected to carry the item at its estimated fair value.

FASB ASC 820-10-35 specifies a hierarchy of valuation techniques based on whether the inputs to those techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. These two types of inputs create the following fair value hierarchy:

- Level 1—Quoted prices (unadjusted) in active markets for identical instruments or liabilities that an entity has the ability to assess at measurement date.
- Level 2—Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; inputs other than quoted prices that are observable for an asset or liability, including interest rates and yield curves observable at commonly quoted intervals, prepayment speeds, loss severities, credit risks and default rates; and market-corroborated inputs.
- Level 3—Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers is unobservable.

This hierarchy requires the Company to use observable market data, when available, and to minimize the use of unobservable inputs when estimating fair value.

As a result of the lack of observable market data resulting from inactive markets, the Company has classified its investment securities available-for-sale, mortgage servicing rights, securitized mortgage collateral and borrowings, derivative assets and liabilities (trust and IRLCs), and long-term debt as Level 3 fair value measurements. Level 3 assets and liabilities measured at fair value on a recurring basis were approximately 87% and 99% and 92% and 99%, respectively, of total assets and total liabilities measured at estimated fair value at September 30, 2017 and December 31, 2016, respectively.

Recurring Fair Value Measurements

The Company assesses the financial instruments on a quarterly basis to determine the appropriate classification within the fair value hierarchy, as defined by ASC Topic 810. Transfers between fair value classifications occur when there are changes in pricing observability levels. Transfers of financial instruments among the levels occur at the beginning of the reporting period. There were no material transfers between our Level 1 and Level 2 classified instruments during the nine months ended September 30, 2017.

[Table of Contents](#)

The following tables present the Company's assets and liabilities that are measured at estimated fair value on a recurring basis, including financial instruments for which the Company has elected the fair value option at September 30, 2017 and December 31, 2016, based on the fair value hierarchy:

	Recurring Fair Value Measurements					
	September 30, 2017			December 31, 2016		
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Assets						
Mortgage loans held-for-sale	\$ —	\$ 572,268	\$ —	\$ —	\$ 388,422	\$ —
Derivative assets, lending, net (1)	—	983	12,015	—	—	11,169
Mortgage servicing rights	—	—	158,950	—	—	131,537
Securitized mortgage collateral	—	—	3,758,140	—	—	4,021,891
Total assets at fair value	\$ —	\$ 573,251	\$ 3,929,105	\$ —	\$ 388,422	\$ 4,164,597
Liabilities						
Securitized mortgage borrowings	\$ —	\$ —	\$ 3,751,831	\$ —	\$ —	\$ 4,017,603
Long-term debt	—	—	44,561	—	—	47,207
Contingent consideration	—	—	5,816	—	—	31,072
Derivative liabilities, lending, net (2)	—	—	—	—	336	—
Total liabilities at fair value	\$ —	\$ —	\$ 3,802,208	\$ —	\$ 336	\$ 4,095,882

- (1) At September 30, 2017, derivative assets, lending, net included \$983 thousand of Hedging Instruments and \$12.0 million of IRLCs and are included in other assets in the accompanying consolidated balance sheets. At December 31, 2016, derivative assets, lending, net included \$11.2 million of IRLCs and is included in other assets in the accompanying consolidated balance sheets.
- (2) At December 31, 2016, derivative liabilities, lending, net included \$336 thousand in Hedging Instruments and is included in other liabilities in the accompanying consolidated balance sheets.

The following tables present reconciliations for all assets and liabilities measured at estimated fair value on a recurring basis using significant unobservable inputs (Level 3) for the three months ended September 30, 2017 and 2016:

	Level 3 Recurring Fair Value Measurements						
	For the Three Months Ended September 30, 2017						
	Investment securities available-for-sale	Securitized mortgage collateral	Securitized mortgage borrowings	Mortgage servicing rights	Interest rate lock commitments, net	Long-term debt	Contingent consideration
Fair value, June 30, 2017	\$ —	\$ 3,776,184	\$ (3,767,519)	\$ 152,273	\$ 9,546	\$ (44,536)	\$ (14,926)
Total gains (losses) included in earnings:							
Interest income (1)	—	9,979	—	—	—	—	—
Interest expense (1)	—	—	(30,810)	—	—	(129)	—
Change in fair value	—	118,384	(122,863)	(11,177)	2,469	104	4,402
Total gains (losses) included in earnings	—	128,363	(153,673)	(11,177)	2,469	(25)	4,402
Transfers in and/or out of Level 3	—	—	—	—	—	—	—
Purchases, issuances and settlements:							
Purchases	—	—	—	—	—	—	—
Issuances	—	—	—	17,854	—	—	—
Settlements	—	(146,407)	169,361	—	—	—	4,708
Fair value, September 30, 2017	\$ —	\$ 3,758,140	\$ (3,751,831)	\$ 158,950	\$ 12,015	\$ (44,561)	\$ (5,816)
Unrealized gains (losses) still held (2)	\$ —	\$ (580,845)	\$ 2,734,962	\$ 158,950	\$ 12,015	\$ (17,439)	\$ (5,816)

- (1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities. Net interest income, including cash received and paid, was \$2.0 million for three months ended September 30, 2017. The difference between accretion of interest income and expense and the amounts of interest income and expense recognized in the consolidated statements of operations is primarily from contractual interest on the securitized mortgage collateral and borrowings.
- (2) Represents the amount of unrealized gains (losses) relating to assets and liabilities classified as Level 3 that are still held and reflected in the fair values at September 30, 2017.

Level 3 Recurring Fair Value Measurements								
For the Three Months Ended September 30, 2016								
	Investment securities available-for-sale	Securitized mortgage collateral	Securitized mortgage borrowings	Derivative liabilities, net, securitized trusts	Mortgage servicing rights	Interest rate lock commitments, net	Long-term debt	Contingent consideration
Fair value, June 30, 2016	\$ 21	\$ 4,290,994	\$ (4,288,585)	\$ (354)	\$ 54,747	\$ 19,303	\$ (30,990)	\$ (49,986)
Total gains (losses) included in earnings:								
Interest income (1)	—	13,336	—	—	—	—	—	—
Interest expense (1)	—	—	(43,956)	—	—	—	(204)	—
Change in fair value	(21)	35,225	(32,644)	(49)	(8,224)	8,017	(8,641)	(24,806)
Total (losses) gains included in earnings	(21)	48,561	(76,600)	(49)	(8,224)	8,017	(8,845)	(24,806)
Transfers in and/or out of Level 3	—	—	—	—	—	—	—	—
Purchases, issuances and settlements:								
Purchases	—	—	—	—	—	—	—	—
Issuances	—	—	—	—	40,890	—	—	—
Settlements	—	(184,098)	213,820	379	—	—	—	14,896
Fair value, September 30, 2016	\$ —	\$ 4,155,457	\$ (4,151,365)	\$ (24)	\$ 87,413	\$ 27,320	\$ (39,835)	\$ (59,896)
Unrealized gains (losses) still held (2)	\$ —	\$ (967,291)	\$ 3,129,974	\$ 9	\$ 87,413	\$ 27,320	\$ 30,928	\$ (59,896)

- (1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities. Net interest income, including cash received and paid, was \$2.6 million for three months ended September 30, 2016. The difference between accretion of interest income and expense and the amounts of interest income and expense recognized in the consolidated statements of operations is primarily from contractual interest on the securitized mortgage collateral and borrowings.
- (2) Represents the amount of unrealized gains (losses) relating to assets and liabilities classified as Level 3 that are still held and reflected in the fair values at September 30, 2016.

The following tables present reconciliations for all assets and liabilities measured at estimated fair value on a recurring basis using significant unobservable inputs (Level 3) for the nine months ended September 30, 2017 and 2016:

Level 3 Recurring Fair Value Measurements								
For the Nine Months Ended September 30, 2017								
	Investment securities available-for-sale	Securitized mortgage collateral	Securitized mortgage borrowings	Mortgage servicing rights	Interest rate lock commitments, net	Long-term debt	Contingent consideration	
Fair value, December 31, 2016	\$ —	\$ 4,021,891	\$ (4,017,603)	\$ 131,537	\$ 11,169	\$ (47,207)	\$ (31,072)	
Total gains (losses) included in earnings:								
Interest income (1)	—	39,564	—	—	—	—	—	—
Interest expense (1)	—	—	(108,010)	—	—	(631)	—	—
Change in fair value	—	219,604	(221,510)	(20,038)	846	(2,657)	9,104	
Total gains (losses) included in earnings	—	259,168	(329,520)	(20,038)	846	(3,288)	9,104	
Transfers in and/or out of Level 3	—	—	—	—	—	—	—	
Purchases, issuances and settlements:								
Purchases	—	—	—	5,618	—	—	—	
Issuances	—	—	—	42,728	—	—	—	
Settlements	—	(522,919)	595,292	(895)	—	5,934	16,152	
Fair value, September 30, 2017	\$ —	\$ 3,758,140	\$ (3,751,831)	\$ 158,950	\$ 12,015	\$ (44,561)	\$ (5,816)	

- (1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities. Net interest income, including cash received and paid, was \$6.1 million for nine months ended September 30, 2017. The difference between accretion of interest income

[Table of Contents](#)

and expense and the amounts of interest income and expense recognized in the consolidated statements of operations is primarily from contractual interest on the securitized mortgage collateral and borrowings.

Level 3 Recurring Fair Value Measurements								
For the Nine Months Ended September 30, 2016								
	Investment securities available-for-sale	Securitized mortgage collateral	Securitized mortgage borrowings	Derivative liabilities, net, securitized trusts	Mortgage servicing rights	Interest rate lock commitments, net	Long-term debt	Contingent consideration
Fair value, December 31, 2015	\$ 26	\$4,574,919	\$(4,578,657)	\$ (1,669)	\$ 36,425	\$ 9,184	\$(31,898)	\$ (48,079)
Total gains (losses) included in earnings:								
Interest income (1)	2	46,540	—	—	—	—	—	—
Interest expense (1)	—	—	(141,927)	—	—	—	(651)	—
Change in fair value	19	27,780	(19,020)	(199)	(32,048)	18,136	(7,286)	(39,813)
Total gains (losses) included in earnings	21	74,320	(160,947)	(199)	(32,048)	18,136	(7,937)	(39,813)
Transfers in and/or out of Level 3	—	—	—	—	—	—	—	—
Purchases, issuances and settlements:								
Purchases	—	—	—	—	—	—	—	—
Issuances	—	—	—	—	91,809	—	—	—
Settlements	(47)	(493,782)	588,239	1,844	(8,773)	—	—	27,996
Fair value, September 30, 2016	\$ —	\$4,155,457	\$(4,151,365)	\$ (24)	\$ 87,413	\$ 27,320	\$(39,835)	\$ (59,896)

- (1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities. Net interest income, including cash received and paid, was \$7.3 million for the nine months ended September 30, 2016. The difference between accretion of interest income and expense and the amounts of interest income and expense recognized in the consolidated statements of operations is primarily from contractual interest on the securitized mortgage collateral and borrowings.

The following table presents quantitative information about the valuation techniques and unobservable inputs applied to Level 3 fair value measurements for financial instruments measured at fair value on a recurring and nonrecurring basis at September 30, 2017:

Financial Instrument	Estimated Fair Value	Valuation Technique	Unobservable Input	Range of Inputs	Weighted Average
Assets and liabilities backed by real estate					
Securitized mortgage collateral, and	\$ 3,758,140	DCF	Prepayment rates	2.1 - 19.0 %	5.6 %
Securitized mortgage borrowings	(3,751,831)		Default rates	0.01 - 4.8 %	1.6 %
			Loss severities	14.0 - 99.8 %	46.3 %
			Discount rates	3.6 - 25.0 %	4.5 %
Other assets and liabilities					
Mortgage servicing rights	\$ 158,950	DCF	Discount rate	9.0 - 14.0 %	9.6 %
			Prepayment rates	8.0 - 84.8 %	10.2 %
Derivative assets - IRLCs, net	12,015	Market pricing	Pull-through rate	15.1 - 99.9 %	82.1 %
Long-term debt	(44,561)	DCF	Discount rate	9.5 %	9.5 %
Contingent consideration	(5,816)	DCF	Discount rate	13.8 %	13.8 %
			Margins	1.5 - 2.0 %	1.7 %
			Probability of outcomes	25.0 - 50.0 %	33.5 %
			(1)		

DCF = Discounted Cash Flow

- (1) Probability of outcomes is the probability of projected CCM earnings over the earn-out period based upon three scenarios (base, low and high).

For assets and liabilities backed by real estate, a significant increase in discount rates, default rates or loss severities would result in a significantly lower estimated fair value. The effect of changes in prepayment speeds would have differing effects depending on the seniority or other characteristics of the instrument. For other assets and liabilities, a significant increase in discount rates would result in a significantly lower estimated fair value. A significant

[Table of Contents](#)

increase in one-month LIBOR would result in a significantly higher estimated fair value for derivative liabilities, net, securitized trusts. The Company believes that the imprecision of an estimate could be significant.

The following tables present the changes in recurring fair value measurements included in net earnings for the three months ended September 30, 2017 and 2016:

Recurring Fair Value Measurements							
Changes in Fair Value Included in Net Earnings							
For the Three Months Ended September 30, 2017							
	Change in Fair Value of						
	Interest Income (1)	Interest Expense (1)	Net Trust Assets	Long- term Debt	Other Revenue and Expense	Gain on sale of loans, net	Total
Investment securities available-for-sale	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Securitized mortgage collateral	9,979	—	118,384	—	—	—	128,363
Securitized mortgage borrowings	—	(30,810)	(122,863)	—	—	—	(153,673)
Derivative liabilities, net, securitized trusts	—	—	—	—	—	—	—
Long-term debt	—	(129)	—	104	—	—	(25)
Mortgage servicing rights (2)	—	—	—	—	(11,177)	—	(11,177)
Contingent consideration (3)	—	—	—	—	4,402	—	4,402
Mortgage loans held-for-sale	—	—	—	—	—	(1,336)	(1,336)
Derivative assets — IRLCs	—	—	—	—	—	2,469	2,469
Derivative liabilities — Hedging Instruments	—	—	—	—	(214)	(758)	(972)
Total	\$ 9,979	\$ (30,939)	\$ (4,479)	\$ 104	\$ (6,989)	\$ 375	\$ (31,949)

- (1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities.
- (2) Included in loss on mortgage servicing rights, net in the consolidated statements of operations.
- (3) Includes \$396 thousand of accretion of the contingent consideration liability.

Recurring Fair Value Measurements							
Changes in Fair Value Included in Net Earnings							
For the Three Months Ended September 30, 2016							
	Change in Fair Value of						
	Interest Income (1)	Interest Expense (1)	Net Trust Assets	Long- term Debt	Other Revenue	Gain on sale of loans, net	Total
Investment securities available-for-sale	\$ —	\$ —	\$ (21)	\$ —	\$ —	\$ —	\$ (21)
Securitized mortgage collateral	13,336	—	35,225	—	—	—	48,561
Securitized mortgage borrowings	—	(43,956)	(32,644)	—	—	—	(76,600)
Derivative liabilities, net, securitized trusts	—	—	(49)(2)	—	—	—	(49)
Long-term debt	—	(204)	—	(8,641)	—	—	(8,845)
Mortgage servicing rights (3)	—	—	—	—	(8,224)	—	(8,224)
Contingent consideration (4)	—	—	—	—	(24,806)	—	(24,806)
Mortgage loans held-for-sale	—	—	—	—	—	5,300	5,300
Derivative assets — IRLCs	—	—	—	—	—	8,017	8,017
Derivative liabilities — Hedging Instruments	—	—	—	—	(96)	(2,181)	(2,277)
Total	\$ 13,336	\$ (44,160)	\$ 2,511	\$ (8,641)	\$ (33,126)	\$ 11,136	\$ (58,944)

- (1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities.
- (2) Included in this amount is \$280 thousand in change in the fair value of derivative instruments, offset by \$329 thousand in cash payments from the securitization trusts for the three months ended September 30, 2016.
- (3) Included in loss on mortgage servicing rights, net in the consolidated statements of operations.
- (4) Includes \$1.6 million of accretion of the contingent consideration liability.

[Table of Contents](#)

The following tables present the changes in recurring fair value measurements included in net earnings for the nine months ended September 30, 2017 and 2016:

Recurring Fair Value Measurements							
Changes in Fair Value Included in Net Earnings							
For the Nine Months Ended September 30, 2017							
Change in Fair Value of							
	Interest	Interest	Net Trust	Long-	Other	Gain on sale	Total
	Income (1)	Expense (1)	Assets	term	Revenue	of loans, net	
				Debt	and Expense		
Investment securities available-for-sale	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Securitized mortgage collateral	39,564	—	219,604	—	—	—	259,168
Securitized mortgage borrowings	—	(108,010)	(221,510)	—	—	—	(329,520)
Derivative liabilities, net, securitized trusts	—	—	—	—	—	—	—
Long-term debt	—	(631)	—	(2,657)	—	—	(3,288)
Mortgage servicing rights (2)	—	—	—	—	(20,038)	—	(20,038)
Contingent consideration (3)	—	—	—	—	9,104	—	9,104
Mortgage loans held-for-sale	—	—	—	—	—	8,262	8,262
Derivative assets — IRLCs	—	—	—	—	—	846	846
Derivative liabilities — Hedging Instruments	—	—	—	—	(296)	1,616	1,320
Total	\$ 39,564	\$ (108,641)	\$ (1,906)(4)	\$ (2,657)	\$ (11,230)	\$ 10,724	\$ (74,146)

- (1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities.
- (2) Included in loss on mortgage servicing rights, net in the consolidated statements of operations.
- (3) Includes \$1.9 million of accretion of the contingent consideration liability.
- (4) For the nine months ended September 30, 2017, change in the fair value of net trust assets, excluding REO was \$1.9 million.

Recurring Fair Value Measurements							
Changes in Fair Value Included in Net Earnings							
For the Nine Months Ended September 30, 2016							
Change in Fair Value of							
	Interest	Interest	Net Trust	Long-	Other	Gain on sale	Total
	Income (1)	Expense (1)	Assets	term	Revenue	of loans, net	
				Debt			
Investment securities available-for-sale	\$ 2	\$ —	\$ 19	\$ —	\$ —	\$ —	\$ 21
Securitized mortgage collateral	46,540	—	27,780	—	—	—	74,320
Securitized mortgage borrowings	—	(141,927)	(19,020)	—	—	—	(160,947)
Derivative liabilities, net, securitized trusts	—	—	(199)(2)	—	—	—	(199)
Long-term debt	—	(651)	—	(7,286)	—	—	(7,937)
Mortgage servicing rights (3)	—	—	—	—	(32,048)	—	(32,048)
Contingent consideration (4)	—	—	—	—	(39,813)	—	(39,813)
Mortgage loans held-for-sale	—	—	—	—	—	19,572	19,572
Derivative assets — IRLCs	—	—	—	—	—	18,136	18,136
Derivative liabilities — Hedging Instruments	—	—	—	—	324	(3,842)	(3,518)
Total	\$ 46,542	\$ (142,578)	\$ 8,580 (5)	\$ (7,286)	\$ (71,537)	\$ 33,866	\$ (132,413)

- (1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities.
- (2) Included in this amount is \$1.5 million in change in the fair value of derivative instruments, offset by \$1.7 million in cash payments from the securitization trusts for the nine months ended September 30, 2016.
- (3) Included in loss on mortgage servicing rights, net in the consolidated statements of operations.
- (4) Includes \$5.2 million of accretion of the contingent consideration liability.
- (5) For the nine months ended September 30, 2016, change in the fair value of net trust assets, excluding REO was \$8.6 million. Excluded from the \$10.3 million change in fair value of net trust assets, excluding REO, in the accompanying consolidated statement of cash flows is \$1.7 million in cash payments from the securitization trusts related to the Company's net derivative liabilities.

[Table of Contents](#)

The following is a description of the measurement techniques for items recorded at estimated fair value on a recurring basis.

Investment securities available-for-sale—Investment securities available-for-sale are carried at fair value. The investment securities consist primarily of non-investment grade mortgage-backed securities. The fair value of the investment securities is measured based upon the Company's expectation of inputs that other market participants would use. Such assumptions include judgments about the underlying collateral, prepayment speeds, future credit losses, forward interest rates and certain other factors. Given the lack of observable market data as of September 30, 2017 and December 31, 2016 relating to these securities, the estimated fair value of the investment securities available-for-sale was measured using significant internal expectations of market participants' assumptions. Investment securities available-for-sale is considered a Level 3 measurement at September 30, 2016.

Mortgage servicing rights—The Company elected to carry its mortgage servicing rights arising from its mortgage loan origination operation at estimated fair value. The fair value of mortgage servicing rights is based upon market prices for similar instruments and a discounted cash flow model. The valuation model incorporates assumptions that market participants would use in estimating the fair value of servicing. These assumptions include estimates of prepayment speeds, discount rate, cost to service, escrow account earnings, contractual servicing fee income, prepayment and late fees, among other considerations. Mortgage servicing rights are considered a Level 3 measurement at September 30, 2017.

Mortgage loans held-for-sale—The Company elected to carry its mortgage loans held-for-sale originated or acquired at estimated fair value. Fair value is based on quoted market prices, where available, prices for other traded mortgage loans with similar characteristics, and purchase commitments and bid information received from market participants. Given the meaningful level of secondary market activity for mortgage loans, active pricing is available for similar assets and accordingly, the Company classifies its mortgage loans held-for-sale as a Level 2 measurement at September 30, 2017.

Securitized mortgage collateral—The Company elected to carry its securitized mortgage collateral at fair value. These assets consist primarily of non-conforming mortgage loans securitized between 2002 and 2007. Fair value measurements are based on the Company's internal models used to compute the net present value of future expected cash flows with observable market participant assumptions, where available. The Company's assumptions include its expectations of inputs that other market participants would use in pricing these assets. These assumptions include judgments about the underlying collateral, prepayment speeds, estimated future credit losses, forward interest rates, investor yield requirements and certain other factors. As of September 30, 2017, securitized mortgage collateral had UPB of \$4.3 billion, compared to an estimated fair value on the Company's balance sheet of \$3.8 billion. The aggregate UPB exceeds the fair value by \$0.5 billion at September 30, 2017. As of September 30, 2017, the UPB of loans 90 days or more past due was \$0.6 billion compared to an estimated fair value of \$0.2 billion. The aggregate UPB of loans 90 days or more past due exceed the fair value by \$0.4 billion at September 30, 2017. Securitized mortgage collateral is considered a Level 3 measurement at September 30, 2017.

Securitized mortgage borrowings—The Company elected to carry its securitized mortgage borrowings at fair value. These borrowings consist of individual tranches of bonds issued by securitization trusts and are primarily backed by non-conforming mortgage loans. Fair value measurements include the Company's judgments about the underlying collateral and assumptions such as prepayment speeds, estimated future credit losses, forward interest rates, investor yield requirements and certain other factors. As of September 30, 2017, securitized mortgage borrowings had an outstanding principal balance of \$4.3 billion, net of \$2.2 billion in bond losses, compared to an estimated fair value of \$3.8 billion. The aggregate outstanding principal balance exceeds the fair value by \$0.5 billion at September 30, 2017. Securitized mortgage borrowings are considered a Level 3 measurement at September 30, 2017.

Contingent consideration—Contingent consideration is applicable to the acquisition of CCM and is estimated and recorded at fair value at the acquisition date as part of purchase price consideration. Additionally, each reporting period, the Company estimates the change in fair value of the contingent consideration and any change in fair value is recognized in the Company's consolidated statements of operations if it is determined to not be a measurement period adjustment. The estimate of the fair value of contingent consideration requires significant judgment and assumptions to

be made about future operating results, discount rates and probabilities of various projected operating result scenarios. During the three months ended September 30, 2017, the change in fair value of contingent consideration was related to a decrease in projected volumes and earnings of CCM. Future revisions to these assumptions could materially change the estimated fair value of contingent consideration and materially affect the Company's financial results. Contingent consideration is considered a Level 3 measurement at September 30, 2017.

Long-term debt—The Company elected to carry all of its long-term debt (consisting of trust preferred securities and junior subordinated notes) at fair value. These securities are measured based upon an analysis prepared by management, which considered the Company's own credit risk, including settlements with trust preferred debt holders and discounted cash flow analysis. As of September 30, 2017, long-term debt had UPB of \$62.0 million compared to an estimated fair value of \$44.6 million. The aggregate UPB exceeds the fair value by \$17.4 million at September 30, 2017. The long-term debt is considered a Level 3 measurement at September 30, 2017.

Derivative assets and liabilities, Securitized trusts—For non-exchange traded contracts, fair value was based on the amounts that would be required to settle the positions with the related counterparties as of the valuation date. Valuations of derivative assets and liabilities were based on observable market inputs, if available. To the extent observable market inputs were not available, fair values measurements include the Company's judgments about future cash flows, forward interest rates and certain other factors, including counterparty risk. Additionally, these values also took into account the Company's own credit standing, to the extent applicable; thus, the valuation of the derivative instrument included the estimated value of the net credit differential between the counterparties to the derivative contract. As of September 30, 2017, there were no derivative assets or liabilities in the securitized trusts. These derivatives were included in the consolidated securitization trusts, which are nonrecourse to the Company, and thus the economic risk from these derivatives was limited to the Company's residual interests in the securitization trusts. Derivative assets and liabilities, securitized trusts were considered a Level 3 measurement in 2016.

Derivative assets and liabilities, Lending—The Company's derivative assets and liabilities are carried at fair value as required by GAAP and are accounted for as free standing derivatives. The derivatives include IRLCs with prospective residential mortgage borrowers whereby the interest rate on the loan is determined prior to funding and the borrowers have locked in that interest rate. These commitments are determined to be derivative instruments in accordance with GAAP. The derivatives also include hedging instruments (typically TBA MBS) used to hedge the fair value changes associated with changes in interest rates relating to its mortgage lending originations as well as mortgage servicing rights. The Company hedges the period from the interest rate lock (assuming a fall-out factor) to the date of the loan sale. The estimated fair value of IRLCs are based on underlying loan types with similar characteristics using the TBA MBS market, which is actively quoted and easily validated through external sources. The data inputs used in this valuation include, but are not limited to, loan type, underlying loan amount, note rate, loan program, and expected sale date of the loan, adjusted for current market conditions. These valuations are adjusted at the loan level to consider the servicing release premium and loan pricing adjustments specific to each loan. For all IRLCs, the base value is then adjusted for the anticipated Pull-through Rate. The anticipated Pull-through Rate is an unobservable input based on historical experience, which results in classification of IRLCs as a Level 3 measurement at September 30, 2017.

The fair value of the Hedging Instruments is based on the actively quoted TBA MBS market using observable inputs related to characteristics of the underlying MBS stratified by product, coupon and settlement date. Therefore, the Hedging Instruments are classified as a Level 2 measurement at September 30, 2017.

[Table of Contents](#)

The following table includes information for the derivative assets and liabilities, lending for the periods presented:

	<u>Notional Amount</u>		<u>Total Gains (Losses) (1)</u> <u>For the Three Months</u> <u>Ended</u>		<u>Total Gains (Losses) (1)</u> <u>For the Nine Months</u> <u>Ended</u>	
	<u>September 30,</u> <u>2017</u>	<u>December 31,</u> <u>2016</u>	<u>September 30,</u>		<u>September 30,</u>	
			<u>2017</u>	<u>2016</u>	<u>2017</u>	<u>2016</u>
Derivative – IRLC's	\$ 650,282	\$ 558,538	\$ 2,469	\$ 8,017	\$ 846	\$ 18,136
Derivative – TBA MBS	544,932	492,157	(2,570)	(5,379)	(3,941)	(21,120)

(1) Amounts included in gain on sale of loans, net within the accompanying consolidated statements of operations.

Nonrecurring Fair Value Measurements

The Company is required to measure certain assets and liabilities at estimated fair value from time to time. These fair value measurements typically result from the application of specific accounting pronouncements under GAAP. The fair value measurements are considered nonrecurring fair value measurements under FASB ASC 820-10.

The following tables present financial and non-financial assets and liabilities measured using nonrecurring fair value measurements at September 30, 2017 and 2016, respectively:

	<u>Nonrecurring Fair Value</u> <u>Measurements</u>			<u>Total Gains (Losses) (1)</u> <u>For the Three Months Ended</u>		<u>Total Gains (Losses) (1)</u> <u>For the Nine Months Ended</u>	
	<u>September 30, 2017</u>			<u>September 30, 2017</u>		<u>September 30, 2017</u>	
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>				
REO (2)	\$ —	\$ 2,870	\$ —	\$ 2,734		\$ 8,484	
Deferred charge (3)	—	—	8,094	(71)		(591)	

- (1) Total losses reflect losses from all nonrecurring measurements during the period.
- (2) Balance represents REO at September 30, 2017 which has been impaired subsequent to foreclosure. For the three and nine months ended September 30, 2017, the Company recorded \$2.7 million and \$8.5 million, respectively, in gains which represents recovery of the net realizable value (NRV) attributable to an improvement in state specific loss severities on properties held during the period which resulted in an increase to NRV.
- (3) For the three and nine months ended September 30, 2017, the Company recorded \$71 thousand and \$591 thousand, respectively, in income tax expense resulting from impairment write-downs of deferred charge based on changes in estimated cash flows and lives of the related mortgages retained in the securitized mortgage collateral.

	<u>Nonrecurring Fair Value</u> <u>Measurements</u>			<u>Total Gains (Losses) (1)</u> <u>For the Three Months Ended</u>		<u>Total Gains (Losses) (1)</u> <u>For the Nine Months Ended</u>	
	<u>September 30, 2016</u>			<u>September 30, 2016</u>		<u>September 30, 2016</u>	
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>				
REO (2)	\$ —	\$ 1,664	\$ —	\$ (1,440)		\$ (5,971)	
Deferred charge (3)	—	—	9,148	(200)		(815)	

- (1) Total losses reflect losses from all nonrecurring measurements during the period.
- (2) Balance represents REO at September 30, 2016 which has been impaired subsequent to foreclosure. For the three and nine months ended September 30, 2016, the Company recorded \$1.4 million and \$6.0 million, respectively, in losses which represent additional impairment write-downs attributable to an increase in state specific loss severities on properties held during the period which resulted in a decrease to NRV.
- (3) For the three and nine months ended September 30, 2016, the Company recorded \$200 thousand and \$815 thousand, respectively, in income tax expense resulting from impairment write-downs of deferred charge based on changes in estimated cash flows and lives of the related mortgages retained in the securitized mortgage collateral.

Real estate owned—REO consists of residential real estate acquired in satisfaction of loans. Upon foreclosure, REO is adjusted to the estimated fair value of the residential real estate less estimated selling and holding costs, offset by

expected contractual mortgage insurance proceeds to be received, if any. Subsequently, REO is recorded at the lower of carrying value or estimated fair value less costs to sell. REO balance representing REOs which have been impaired subsequent to foreclosure are subject to nonrecurring fair value measurement and included in the nonrecurring fair value measurements tables. Fair values of REO are generally based on observable market inputs, and considered Level 2 measurements at September 30, 2017.

Deferred charge— Deferred charge represents the deferral of income tax expense on inter-company profits that resulted from the sale of mortgages from taxable subsidiaries to IMH in prior years. The Company evaluates the deferred charge for impairment quarterly using internal estimates of estimated cash flows and lives of the related mortgages retained in the securitized mortgage collateral. If the deferred charge is determined to be impaired, it is recognized as a component of income tax expense. Deferred charge is considered a Level 3 measurement at September 30, 2017.

Note 7.—Income Taxes

The Company calculates its quarterly tax provision pursuant to the guidelines in ASC 740 Income Taxes. ASC 740 requires companies to estimate the annual effective tax rate for current year ordinary income. In calculating the effective tax rate, permanent differences between financial reporting and taxable income are factored into the calculation, but temporary differences are not. The estimated annual effective tax rate represents the best estimate of the tax provision in relation to the best estimate of pre-tax ordinary income or loss. The estimated annual effective tax rate is then applied to year-to-date ordinary income or loss to calculate the year-to-date interim tax provision.

The Company recorded income tax expense of \$2.1 million and \$3.6 million for the three and nine months ended September 30, 2017, respectively, primarily the result of the recognition of a deferred tax liability created by the amortization of an indefinite-life intangible asset (goodwill) and amortization of the deferred charge. The deferred tax liability for indefinite-life intangibles cannot be included in the calculation of valuation allowance as these liabilities cannot be considered when determining the realizability of the net deferred tax assets.

For the three and nine months ended September 30, 2016, the Company recorded income tax benefit of \$130 thousand and expense of \$728 thousand, respectively, primarily the result of a return to provision adjustment for the 2015 tax return booked in the third quarter, amortization of the deferred charge, federal alternative minimum tax (AMT), and state income taxes from states where the Company does not have net operating loss carryforwards or state minimum taxes, including AMT. The deferred charge represents the deferral of income tax expense on inter-company profits that resulted from the sale of mortgages from taxable subsidiaries to IMH prior to 2008. The deferred charge amortization and/or impairment, which does not result in any tax liability to be paid, is calculated based on the change in the estimated fair value of the underlying securitized mortgage collateral during the period. The deferred charge is included in other assets in the accompanying consolidated balance sheets and is amortized as a component of income tax expense in the accompanying consolidated statements of operations.

As of December 31, 2016, the Company had estimated federal net operating loss (NOL) carryforwards of approximately \$581.8 million. Federal net operating loss carryforwards begin to expire in 2027. As of December 31, 2016, the Company had estimated California net operating loss (NOL) carryforwards of approximately \$487.0 million, of which \$86.9 million expire in 2017. The Company may not be able to realize the maximum benefit due to the nature and tax entity that holds the NOL.

Note 8.—Reconciliation of Earnings Per Share

Basic net earnings per share is computed by dividing net earnings available to common stockholders (numerator) by the weighted average number of vested, common shares outstanding during the period (denominator). Diluted net earnings per share is computed on the basis of the weighted average number of shares of common stock outstanding plus the effect of dilutive potential common shares outstanding during the period using the if-converted

[Table of Contents](#)

method. Dilutive potential common shares include shares issuable upon conversion of Convertible Notes, dilutive effect of outstanding stock options and deferred stock units (DSUs).

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2017	2016	2017	2016
Numerator for basic earnings per share:				
Net earnings	\$ 2,317	\$ 16,498	\$ 13,384	\$ 29,729
Numerator for diluted earnings per share:				
Net earnings	\$ 2,317	\$ 16,498	\$ 13,384	\$ 29,729
Interest expense attributable to convertible notes (1)	—	457	1,158	1,997
Net earnings plus interest expense attributable to convertible notes	\$ 2,317	\$ 16,955	\$ 14,542	\$ 31,726
Denominator for basic earnings per share (2):				
Basic weighted average common shares outstanding during the period	20,916	12,920	18,928	12,241
Denominator for diluted earnings per share (2):				
Basic weighted average common shares outstanding during the period	20,916	12,920	18,928	12,241
Net effect of dilutive convertible notes (1)	—	1,163	1,163	1,426
Net effect of dilutive stock options and DSU's	279	320	290	306
Diluted weighted average common shares	21,195	14,403	20,381	13,973
Net earnings per common share:				
Basic	\$ 0.11	\$ 1.28	\$ 0.71	\$ 2.43
Diluted	\$ 0.11	\$ 1.18	\$ 0.71	\$ 2.27

- (1) Adjustments to diluted earnings per share for the convertible notes for the three months ended September 30, 2017 were excluded from the calculation as they are anti-dilutive.
(2) Number of shares presented in thousands.

For September 30, 2017, there were 1.2 million anti-dilutive stock options outstanding. There were 842 thousand anti-dilutive stock options outstanding for the three and nine months ended September 30, 2016.

Note 9.—Segment Reporting

The Company has three primary reporting segments which include mortgage lending, real estate services and long-term mortgage portfolio. Unallocated corporate and other administrative costs, including the costs associated with being a public company, are presented in Corporate and other.

Statement of Operations Items for the	Mortgage	Real Estate	Long-term	Corporate	
Three Months Ended September 30, 2017:	Lending	Services	Portfolio	and other	Consolidated
Gain on sale of loans, net	\$ 42,476	\$ —	\$ —	\$ —	\$ 42,476
Real estate services fees, net	—	1,355	—	—	1,355
Servicing fees, net	8,492	—	—	—	8,492
Loss on mortgage servicing rights, net	(10,513)	—	—	—	(10,513)
Other revenue	—	—	81	185	266
Accretion of contingent consideration	(396)	—	—	—	(396)
Change in fair value of contingent consideration	4,798	—	—	—	4,798
Loss on extinguishment of debt	—	—	—	—	—
Other operating expense	(36,663)	(797)	(67)	(4,435)	(41,962)
Other income (expense)	1,107	—	(722)	(480)	(95)
Net earnings (loss) before income tax expense	<u>\$ 9,301</u>	<u>\$ 558</u>	<u>\$ (708)</u>	<u>\$ (4,730)</u>	<u>4,421</u>
Income tax expense					2,104
Net earnings					<u>\$ 2,317</u>

Statement of Operations Items for the	Mortgage	Real Estate	Long-term	Corporate	
Three Months Ended September 30, 2016:	Lending	Services	Portfolio	and other	Consolidated
Gain on sale of loans, net	\$ 113,158	\$ —	\$ —	\$ —	\$ 113,158
Real estate services fees, net	—	2,678	—	—	2,678
Servicing fees, net	3,789	—	—	—	3,789
Loss on mortgage servicing rights, net	(15,857)	—	—	—	(15,857)
Other revenue	18	—	71	136	225
Accretion of contingent consideration	(1,591)	—	—	—	(1,591)
Change in fair value of contingent consideration	(23,215)	—	—	—	(23,215)
Other operating expense	(53,884)	(2,005)	(102)	(562)	(56,553)
Other income (expense)	1,092	—	(6,075)	(1,283)	(6,266)
Net earnings (loss) before income tax expense	<u>\$ 23,510</u>	<u>\$ 673</u>	<u>\$ (6,106)</u>	<u>\$ (1,709)</u>	<u>\$ 16,368</u>
Income tax benefit					(130)
Net earnings					<u>\$ 16,498</u>

[Table of Contents](#)

Statement of Operations Items for the Nine Months Ended September 30, 2017:	Mortgage Lending	Real Estate Services	Long-term Portfolio	Corporate and other	Consolidated
Gain on sale of loans, net	\$ 116,602	\$ —	\$ —	\$ —	\$ 116,602
Real estate services fees, net	—	4,492	—	—	4,492
Servicing fees, net	23,575	—	—	—	23,575
Loss on mortgage servicing rights, net	(18,159)	—	—	—	(18,159)
Other revenue	19	—	209	313	541
Accretion of contingent consideration	(1,948)	—	—	—	(1,948)
Change in fair value of contingent consideration	11,052	—	—	—	11,052
Loss on extinguishment of debt	—	—	(1,265)	—	(1,265)
Other operating expense	(109,979)	(2,534)	(253)	(12,176)	(124,942)
Other income (expense)	2,096	—	6,673	(1,758)	7,011
Net earnings (loss) before income tax expense	\$ 23,258	\$ 1,958	\$ 5,364	\$ (13,621)	16,959
Income tax expense	—	—	—	—	3,575
Net earnings	—	—	—	—	\$ 13,384

Statement of Operations Items for the Nine Months Ended September 30, 2016:	Mortgage Lending	Real Estate Services	Long-term Portfolio	Corporate and other	Consolidated
Gain on sale of loans, net	\$ 245,849	\$ —	\$ —	\$ —	\$ 245,849
Real estate services fees, net	—	6,773	—	—	6,773
Servicing fees, net	8,680	—	—	—	8,680
Loss on mortgage servicing rights, net	(41,249)	—	—	—	(41,249)
Other revenue	70	—	183	200	453
Accretion of contingent consideration	(5,244)	—	—	—	(5,244)
Change in fair value of contingent consideration	(34,569)	—	—	—	(34,569)
Other operating expense	(138,269)	(5,228)	(347)	(3,751)	(147,595)
Other income (expense)	2,148	—	(418)	(4,371)	(2,641)
Net earnings (loss) before income tax expense	\$ 37,416	\$ 1,545	\$ (582)	\$ (7,922)	\$ 30,457
Income tax expense	—	—	—	—	728
Net earnings	—	—	—	—	\$ 29,729

Balance Sheet Items as of:	Mortgage Lending	Real Estate Services	Long-term Mortgage Portfolio	Corporate and other	Consolidated
Total Assets at September 30, 2017 (1)	\$ 1,008,628	\$ 555	\$ 3,777,326	\$ 28,868	\$ 4,815,377
Total Assets at December 31, 2016 (1)	\$ 762,924	\$ 5,451	\$ 4,042,273	\$ 53,086	\$ 4,863,734

(1) All segment asset balances exclude intercompany balances.

Note 10.—Commitments and Contingencies

Legal Proceedings

The Company is a defendant in or a party to a number of legal actions or proceedings that arise in the ordinary course of business. In some of these actions and proceedings, claims for monetary damages are asserted against the Company. In view of the inherent difficulty of predicting the outcome of such legal actions and proceedings, the Company generally cannot predict what the eventual outcome of the pending matters will be, what the timing of the ultimate resolution of these matters will be, or what the eventual loss related to each pending matter may be, if any.

In accordance with applicable accounting guidance, the Company establishes an accrued liability for litigation when those matters present loss contingencies that are both probable and estimable. In any case, there may be an exposure to losses in excess of any such amounts whether accrued or not. Any estimated loss is subject to significant

[Table of Contents](#)

judgment and is based upon currently available information, a variety of assumptions, and known and unknown uncertainties. The matters underlying the estimated loss will change from time to time, and actual results may vary significantly from the current estimate. Therefore, an estimate of possible loss represents what the Company believes to be an estimate of possible loss only for certain matters meeting these criteria. It does not represent the Company's maximum loss exposure.

Based on the Company's current understanding of these pending legal actions and proceedings, management does not believe that judgments or settlements arising from pending or threatened legal matters, individually or in the aggregate, will have a material adverse effect on the consolidated financial position, operating results or cash flows of the Company. However, in light of the inherent uncertainties involved in these matters, some of which are beyond the Company's control, and the very large or indeterminate damages sought in some of these matters, an adverse outcome in one or more of these matters could be material to the Company's results of operations or cash flows for any particular reporting period.

The legal matter updates summarized below are ongoing and may have an effect on the Company's business and future financial condition and results of operations:

On April 30, 2012, a purported class action was filed entitled *Marentes v. Impac Mortgage Holdings, Inc.*, alleging that certain loan modification activities of the Company constitute an unfair business practice, false advertising and marketing, and that the fees charged are improper. The complaint seeks unspecified damages, restitution, injunctive relief, attorney's fees and prejudgment interest. Phase one of the trial for this matter has been continued, with the parties scheduled to return to court on November 29, 2017, for a status conference.

The Company is a party to other litigation and claims which are normal in the course of our operations. While the results of such other litigation and claims cannot be predicted with certainty, we believe the final outcome of such matters will not have a material adverse effect on our financial condition or results of operations. The Company believes that it has meritorious defenses to the claims and intends to defend these claims vigorously and as such the Company believes the final outcome of such matters will not have a material adverse effect on its financial condition or results of operations. Nevertheless, litigation is uncertain and the Company may not prevail in the lawsuits and can express no opinion as to their ultimate resolution. An adverse judgment in any of these matters could have a material adverse effect on the Company's financial position and results of operations.

Please refer to IMH's report on Form 10-K for the year ended December 31, 2016 and subsequent quarterly reports for a description of litigation and claims.

Repurchase Reserve

When the Company sells mortgage loans, it makes customary representations and warranties to the purchasers about various characteristics of each loan such as the origination and underwriting guidelines, including but not limited to the validity of the lien securing the loan, property eligibility, borrower credit, income and asset requirements, and compliance with applicable federal, state and local law. The Company's whole loan sale agreements generally require it to repurchase loans if the Company breached a representation or warranty given to the loan purchaser.

The following table summarizes the repurchase reserve activity, within other liabilities on the consolidated balance sheets, related to previously sold loans for the nine months ended September 30, 2017 and year ended December 31, 2016:

	September 30, 2017	December 31, 2016
Beginning balance	\$ 5,408	\$ 5,236
Provision for repurchases	192	379
Settlements	(620)	(207)
Total repurchase reserve	<u>\$ 4,980</u>	<u>\$ 5,408</u>

Short-Term Loan Commitments

The Company uses a portion of its warehouse borrowing capacity to provide secured short-term revolving financing to small and medium-size mortgage originators to finance mortgage loans from the closing of the mortgage loans until sold to investors (Finance Receivables). As of September 30, 2017, the warehouse lending operations had warehouse lines to non-affiliated customers totaling \$159.0 million, of which there was an outstanding balance of \$60.9 million in finance receivables compared to \$62.9 million as of December 31, 2016. The finance receivables are generally secured by residential mortgage loans as well as personal guarantees.

Commitments to Extend Credit

The Company enters into IRLCs with prospective borrowers whereby the Company commits to lend a certain loan amount under specific terms and interest rates to the borrower. These loan commitments are treated as derivatives and are carried at fair value. See Note 6. — Fair value of Financial Instruments for more information.

Note 11.—Equity and Share Based Payments

Equity

On April 18, 2017, the Company and certain purchasers entered into a securities purchase agreement, pursuant to which the Company sold \$56.0 million worth of shares of its common stock in a registered direct offering (Offering) at a price of \$12.66 per share. In the Offering, the Company issued an aggregate of 4,423,381 shares of common stock.

The net proceeds to the Company from the Offering were approximately \$55.5 million after deducting the financial advisory fee and estimated aggregate offering expenses payable by the Company. The Company used a portion of the proceeds from the Offering for general corporate purposes, including general administrative expenses and working capital and capital expenditures, development costs, and repayment of debt.

As further described in Note 4. – Debt, Convertible Notes, in January 2016, the Company elected to exercise its option to convert the Notes to common stock. The conversion resulted in the Company issuing an aggregate of 1,839,080 shares of common stock at a conversion price of \$10.875 per share.

Share Based Payments

The following table summarizes activity, pricing and other information for the Company's stock options for the nine months ended September 30, 2017:

	Number of Shares	Weighted- Average Exercise Price
Options outstanding at beginning of year	1,391,327	\$ 13.37
Options granted	358,450	13.72
Options exercised	(89,537)	6.36
Options forfeited/cancelled	(26,355)	16.95
Options outstanding at end of period	<u>1,633,885</u>	13.77
Options exercisable at end of period	<u>947,479</u>	\$ 12.24

As of September 30, 2017, there was approximately \$4.1 million of total unrecognized compensation cost related to stock option compensation arrangements granted under the plan, net of estimated forfeitures. That cost is expected to be recognized over the remaining weighted average period of 2.1 years.

There were 358,450 and 342,000 options granted during the nine months ended September 30, 2017 and 2016, respectively. For the nine months ended September 30, 2017 and 2016, the aggregate grant-date fair value of stock options granted was approximately \$2.2 million and \$2.7 million, respectively.

[Table of Contents](#)

The following table summarizes activity, pricing and other information for the Company's DSU's, also referred to as deferred stock units as the issuance of the stock is deferred until termination of service, for the nine months ended September 30, 2017:

	Number of Shares	Weighted- Average Grant Date Fair Value
DSU's outstanding at beginning of year	85,750	\$ 9.83
DSU's granted	15,000	13.72
DSU's exercised	—	—
DSU's forfeited/cancelled	—	—
DSU's outstanding at end of period	<u>100,750</u>	<u>\$ 10.41</u>

As of September 30, 2017, there was approximately \$252 thousand of total unrecognized compensation cost related to the DSU compensation arrangements granted under the plan. That cost is expected to be recognized over a weighted average period of 2.7 years.

Note 12.—Subsequent Events

Subsequent events have been evaluated through the date of this filing.

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

(dollars in thousands, except per share data or as otherwise indicated)

Unless the context otherwise requires, the terms “Company,” “we,” “us,” and “our” refer to Impac Mortgage Holdings, Inc. (the Company or IMH), a Maryland corporation incorporated in August 1995, and its subsidiaries, Integrated Real Estate Service Corporation (IRES), Impac Mortgage Corp. (IMC), IMH Assets Corp. (IMH Assets), and Impac Funding Corporation (IFC).

Forward-Looking Statements

This report on Form 10-Q contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements, some of which are based on various assumptions and events that are beyond our control, may be identified by reference to a future period or periods or by the use of forward-looking terminology, such as “may,” “will,” “believe,” “expect,” “likely,” “should,” “could,” “seem to,” “anticipate,” “plan,” “intend,” “project,” “assume,” or similar terms or variations on those terms or the negative of those terms. The forward-looking statements are based on current management expectations. Actual results may differ materially as a result of several factors, including, but not limited to the following: failure to increase origination volume and ability to successfully leverage our marketing platform to expand volumes of our other loan products; successful development, marketing, sale and financing of new mortgage products, including expansion of non-Qualified Mortgage originations and government loan programs; inability to successfully reduce prepayment on our mortgage loans, ability to successfully diversify our loan products; ability to increase our market share and geographic footprint in the various residential mortgage businesses; ability to manage and sell MSRs as needed; volatility in the mortgage industry; unexpected interest rate fluctuations and margin compression; our ability to manage personnel expenses in relation to mortgage production levels; our ability to successfully use warehousing capacity; increased competition in the mortgage lending industry by larger or more efficient companies; issues and system risks related to our technology; ability to successfully create cost and product efficiencies through new technology; more than expected increases in default rates or loss severities and mortgage related losses; ability to obtain additional financing, through lending and repurchase facilities, debt or equity funding, strategic relationships or otherwise; the terms of any financing, whether debt or equity, that we do obtain and our expected use of proceeds from any financing; increase in loan repurchase requests and ability to adequately settle repurchase obligations; failure to create brand awareness; the outcome, including any settlements, of litigation or regulatory actions pending against us or other legal contingencies; and our compliance with applicable local, state and federal laws and regulations and other general market and economic conditions.

For a discussion of these and other risks and uncertainties that could cause actual results to differ from those contained in the forward-looking statements, see “Risk Factors” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in the Company’s Annual Report on Form 10-K for the period ended December 31, 2016, and other reports we file under the Securities Exchange Act of 1934. This document speaks only as of its date and we do not undertake, and specifically disclaim any obligation, to release publicly the results of any revisions that may be made to any forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date of such statements.

The Mortgage Industry and Discussion of Relevant Fiscal Periods

The mortgage industry is subject to current events that occur in the financial services industry including changes to regulations and compliance requirements that result in uncertainty surrounding the actions of states, municipalities and new government agencies, including the Consumer Financial Protection Bureau (CFPB) and Federal Housing Finance Agency (FHFA). These events can also include changes in economic indicators, interest rates, price competition, geographic shifts, disposable income, housing prices, market liquidity, market anticipation, environmental conditions, such as hurricanes and floods, and customer perception, as well as others. The factors that affect the industry change rapidly and can be unforeseeable making it difficult to predict and manage an operation in the financial services industry.

Current events can diminish the relevance of “quarter over quarter” and “year-to-date over year-to-date” comparisons of financial information. In such instances, we attempt to present financial information in Management’s Discussion and Analysis of Financial Condition and Results of Operations that is the most relevant to our financial information.

Selected Financial Results

	For the Three Months Ended			For the Nine Months Ended	
	September 30, 2017	June 30, 2017	September 30, 2016	September 30, 2017	September 30, 2016
Revenues:					
Gain on sale of loans, net	\$ 42,476	\$ 36,806	\$ 113,158	\$ 116,602	\$ 245,849
Real estate services fees, net	1,355	1,504	2,678	4,492	6,773
Servicing fees, net	8,492	7,764	3,789	23,575	8,680
Loss on mortgage servicing rights, net	(10,513)	(6,669)	(15,857)	(18,159)	(41,249)
Other	266	228	225	541	453
Total revenues	42,076	39,633	103,993	127,051	220,506
Expenses:					
Personnel expense	23,062	21,373	38,467	69,353	93,025
Business promotion	10,403	10,110	10,350	30,744	30,828
General, administrative and other	8,497	8,324	7,736	24,845	23,742
Accretion of contingent consideration	396	707	1,591	1,948	5,244
Change in fair value of contingent consideration	(4,798)	(6,793)	23,215	(11,052)	34,569
Total expenses	37,560	33,721	81,359	115,838	187,408
Operating income:	4,516	5,912	22,634	11,213	33,098
Other income (expense):					
Net interest income	1,546	1,098	1,304	3,090	2,036
Loss on extinguishment of debt	—	(1,265)	—	(1,265)	—
Change in fair value of long-term debt	104	(265)	(8,641)	(2,657)	(7,286)
Change in fair value of net trust assets	(1,745)	2,005	1,071	6,578	2,609
Total other income (expense)	(95)	1,573	(6,266)	5,746	(2,641)
Net earnings before income taxes	4,421	7,485	16,368	16,959	30,457
Income tax expense	2,104	1,045	(130)	3,575	728
Net earnings	\$ 2,317	\$ 6,440	\$ 16,498	\$ 13,384	\$ 29,729
Diluted weighted average common shares	21,195	21,258	14,403	20,381	13,973
Diluted earnings per share	\$ 0.11	\$ 0.32	\$ 1.18	\$ 0.71	\$ 2.27

Status of Operations

Summary Highlights

- Mortgage lending volumes increased in the third quarter of 2017 to \$2.1 billion from \$1.8 billion in the second quarter of 2017, but decreased as compared to \$4.2 billion in the third quarter of 2016.
- Mortgage servicing portfolio increased to \$15.7 billion at September 30, 2017 from \$14.7 billion at June 30, 2017 and \$9.5 billion at September 30, 2016.
- Servicing fees, net increased to \$8.5 million for the three months ended September 30, 2017 from \$7.8 million for the three months ended June 30, 2017 and \$3.8 million for the three months ended September 30, 2016.
- NonQM mortgage origination volumes increased in the third quarter of 2017 to \$239.4 million from \$232.5 million in the second quarter of 2017 and \$68.9 million in the third quarter of 2016.

For the third quarter of 2017, we reported net earnings of \$2.3 million, or \$0.11 per diluted common share, as compared to net earnings of \$16.5 million, or \$1.18 per diluted common share, for the third quarter of 2016. For the third quarter of 2017, operating income, excluding the changes in contingent consideration (adjusted operating (loss) income (loss)) was \$114 thousand, or \$0.01 per diluted common share, as compared to \$47.4 million, or \$3.29 per diluted common share, for the third quarter of 2016. The decrease in net earnings and adjusted operating income (loss)

[Table of Contents](#)

was primarily due to a decline in gain on sale of loans revenues in the third quarter of 2017 as compared to third quarter of 2016. The decline in gain on sale of loans revenues was due to a decrease in origination volume magnified also by the decline in gain on sale margins. Origination volume declined 51% in the third quarter of 2017 as compared to the same period in the prior year (discussed further below). Gain on sale margins decreased by 64 basis point (bps) to 204 bps in the third quarter of 2017, as compared to 268 bps in the third quarter of 2016 reflecting the margin compression resulting from the historically low interest rate environment in the third quarter of 2016, in which the Company was able to generate significantly larger volume with wide gain on sale margins.

Net earnings include fair value adjustments for changes in the contingent consideration, long-term debt and net trust assets. The contingent consideration is related to the CashCall Mortgage (CCM) acquisition transaction, while the other fair value adjustments are related to our legacy portfolio. These fair value adjustments are non-cash items and are not related to current operating results. Although we are required to record change in fair value and accretion of the contingent consideration, management believes operating income excluding contingent consideration changes and the related accretion is more useful to discuss our ongoing and future operations.

Adjusted operating income (loss) is not considered an accounting principle generally accepted in the United States of America (GAAP) financial measurement; see the discussion and reconciliation on non-GAAP financial measures below.

We calculate adjusted operating income (loss) and adjusted operating income per share as performance measures, which are considered non-GAAP financial measures, to further aid our investors in understanding and analyzing our core operating results and comparing them among periods. Adjusted operating income (loss) and adjusted operating income (loss) per share exclude certain items that we do not consider part of our core operating results. These non-GAAP financial measures are not intended to be considered in isolation or as a substitute for net earnings before income taxes, net earnings or diluted earnings per share (EPS) prepared in accordance with GAAP. The table below shows operating income excluding these items:

	For the Three Months Ended			For the Nine Months Ended	
	September 30, 2017	June 30, 2017	September 30, 2016	September 30, 2017	September 30, 2016
Net earnings:	\$ 2,317	\$ 6,440	\$ 16,498	\$ 13,384	\$ 29,729
Total other (income) expense	95	(1,573)	6,266	(5,746)	2,641
Income tax expense	2,104	1,045	(130)	3,575	728
Operating income:	\$ 4,516	\$ 5,912	\$ 22,634	\$ 11,213	\$ 33,098
Accretion of contingent consideration	396	707	1,591	1,948	5,244
Change in fair value of contingent consideration	(4,798)	(6,793)	23,215	(11,052)	34,569
Adjusted operating income (loss)	\$ 114	\$ (174)	\$ 47,440	\$ 2,109	\$ 72,911
Diluted weighted average common shares	21,195	21,258	14,403	20,381	13,973
Diluted adjusted operating income (loss) per share	\$ 0.01	\$ (0.01)	\$ 3.29	\$ 0.10	\$ 5.22
Diluted earnings per share	\$ 0.11	\$ 0.32	\$ 1.18	\$ 0.71	\$ 2.27
Adjustments:					
Total other (expense) income (1)	—	(0.09)	0.40	(0.35)	0.05
Income tax expense	0.10	0.05	(0.01)	0.18	0.05
Accretion of contingent consideration	0.02	0.03	0.11	0.10	0.38
Change in fair value of contingent consideration	(0.22)	(0.32)	1.61	(0.54)	2.47
Diluted adjusted operating income (loss) per share	\$ 0.01	\$ (0.01)	\$ 3.29	\$ 0.10	\$ 5.22

- (1) Except for when anti-dilutive, convertible debt interest expense, net of tax, is included for calculating diluted earnings per share (EPS) and is excluded for purposes of reconciling GAAP diluted EPS to non-GAAP diluted adjusted operating income (loss) per share.

Originations

(in millions)	For the Three Months Ended				
	September 30, 2017	June 30, 2017	% Change	September 30, 2016	% Change
Retail	\$ 1,426.2	\$ 1,186.8	20 %	\$ 3,273.7	(56)%
Correspondent	376.4	305.8	23	583.2	(35)
Wholesale	281.7	301.0	(6)	360.1	(22)
Total originations	<u>\$ 2,084.3</u>	<u>\$ 1,793.6</u>	16	<u>\$ 4,217.0</u>	(51)

During the third quarter of 2017, total originations increased 16% to \$2.1 billion as compared to \$1.8 billion in the second quarter of 2017 and decreased 51% as compared to \$4.2 billion in the third quarter of 2016. This increase from the second quarter of 2017 was the result of a slight decline in mortgage interest rates during the third quarter of 2017. The decrease in originations from the third quarter of 2016 was a result of higher interest rates during the third quarter of 2017 as compared to the historically low interest rate environment the previous year, causing a sharp drop in refinance volume.

Our loan products primarily include conventional loans eligible for sale to Fannie Mae and Freddie Mac, loans eligible for government insurance (government loans) by the Federal Housing Administration (FHA), Veterans Affairs (VA), United States Department of Agriculture (USDA) and also NonQM mortgages.

Originations by Loan Type:

(in millions)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2017	2016	2017	2016
Conventional	\$ 1,345.2	\$ 3,707.1	\$ 3,391.8	\$ 8,322.9
Government (1)	499.7	439.2	1,409.9	1,281.7
NonQM	239.4	68.9	656.2	203.3
Other	—	1.8	—	5.7
Total originations	<u>\$ 2,084.3</u>	<u>\$ 4,217.0</u>	<u>\$ 5,457.9</u>	<u>\$ 9,813.6</u>

(1) Includes all government-insured loans including FHA, VA and USDA.

During the third quarter of 2017, the origination volume of NonQM loans increased to \$239.4 million, as compared to \$232.5 million in the second quarter of 2017 and \$68.9 million in the third quarter of 2016. In the third quarter of 2017, NonQM origination volumes by channel were \$61.8 million from the retail channel and \$177.6 million from the wholesale and correspondent channels. In the second quarter of 2017, retail NonQM originations were \$82.9 million while wholesale and correspondent originations were \$149.6 million. The NonQM loans originated in 2016 and through the third quarter of 2017 have all been sold on a servicing released basis.

We believe there is an underserved mortgage market for borrowers with good credit who may not meet the qualified mortgage (QM) guidelines set out by the Consumer Financial Protection Bureau (CFPB). During 2014, we began originating NonQM loans. We have established strict lending guidelines, including determining the prospective borrowers' ability to repay the mortgage, which we believe will keep delinquencies and foreclosures at acceptable levels. We continue to refine our guidelines to expand our reach to the underserved market of credit worthy borrowers who can fully document and substantiate an ability to repay mortgage loans, but are unable to obtain financing through traditional programs (QM loans), for example self-employed borrowers. Through the third quarter of 2017, our NonQM origination volume was \$656.2 million with an average Fair Isaac Company credit score (FICO) of 726 and a weighted average loan to value ratio (LTV) of 64%.

[Table of Contents](#)

In 2016, we relaunched our NonQM loan program as “The Intelligent NonQM Mortgage,” to better communicate our NonQM loan value proposition to consumers, brokers, sellers and investors. In conjunction with this product, we have established investor relationships that provide us with an exit strategy for these nonconforming loans.

(in millions)	For the Three Months Ended				For the Nine Months Ended			
	September 30,				September 30,			
	2017	%	2016	%	2017	%	2016	%
Refinance	\$ 1,589.8	76 %	\$ 3,756.8	89 %	\$ 4,183.9	77 %	\$ 8,554.0	87 %
Purchase	494.5	24	460.2	11	1,274.0	23	1,259.6	13
Total originations	<u>\$ 2,084.3</u>	<u>100</u>	<u>\$ 4,217.0</u>	<u>100</u>	<u>\$ 5,457.9</u>	<u>100</u>	<u>\$ 9,813.6</u>	<u>100</u>

During the third quarter of 2017, refinance volume decreased approximately 58% to \$2.2 billion as compared to \$4.2 billion in the third quarter of 2016 as a result of rising interest rates at the end of 2016 and continuing in the first quarter of 2017. Despite the 51% decrease in origination volumes during the third quarter of 2017, purchase money transactions increased 7% to \$494.5 million as compared to \$460.2 million in the third quarter of 2016.

Mortgage servicing portfolio

(in millions)	September 30, 2017	June 30, 2017	% Change	September 30, 2016	% Change
Mortgage servicing portfolio	\$ 15,703.1	\$ 14,667.9	7 %	\$ 9,450.7	66 %

The mortgage servicing portfolio increased to \$15.7 billion at September 30, 2017 as compared to \$14.7 billion at June 30, 2017 and \$9.5 billion at September 30, 2016. The increase was due to a shift in our strategy in 2016 to retain our mortgage servicing as well as initiating a retention program to recapture portfolio runoff during the low interest rate environment. During 2017, we have continued with our strategy of growing the mortgage servicing portfolio. During the nine months ended September 30, 2017, the mortgage servicing portfolio increased due to servicing retained loan sales of \$4.7 billion in unpaid principal balance (UPB) as well as a purchase of approximately \$570.0 million in UPB of mortgage servicing rights (MSR). As a result, the UPB of our mortgage servicing portfolio increased 66% to \$15.7 billion as of September 30, 2017 from September 30, 2016. The servicing portfolio generated net servicing fees of \$8.5 million in the third quarter of 2017, a 124% increase over the net servicing fees of \$3.8 million in the third quarter of 2016. Delinquencies within the servicing portfolio have increased slightly but remain low at 0.49% for 60+ days delinquent as of September 30, 2017 as compared to 0.25% as of December 31, 2016. With the acquisition of MSRs in the second quarter of 2017, we added Specialized Loan Servicing LLC as a subservicer in addition to our current subservicer LoanCare, LLC.

The following table includes information about our mortgage servicing portfolio:

(in millions)	At September 30, 2017	% 60+ days delinquent (1)	At December 31, 2016	% 60+ days delinquent (1)
Fannie Mae	\$ 7,501.2	0.21 %	\$ 6,204.2	0.12 %
Freddie Mac	5,680.3	0.15	4,611.8	0.08
Ginnie Mae	2,519.6	1.88	1,359.5	1.25
Other	2.0	16.67	176.0	0.00
Total servicing portfolio	<u>\$ 15,703.1</u>	<u>0.49</u>	<u>\$ 12,351.5</u>	<u>0.25</u>

(1) Based on loan count.

During the nine months ended September 30, 2017, our warehouse borrowing capacity increased from \$925.0 million to \$960.0 million. In addition to funding our mortgage loan originations, we also used a portion of our warehouse borrowing capacity to provide re-warehouse facilities to our customers, correspondent sellers and other small mortgage banking companies represented as finance receivables on the consolidated balance sheets. The outstanding balance of finance receivables decreased to \$60.9 million at September 30, 2017 as compared to \$62.9 million at

December 31, 2016. The warehouse lending division funding volumes increased to \$279.7 million during the third quarter of 2017 as compared to \$251.0 million for the second quarter of 2017 but decreased compared to \$286.9 million for the third quarter of 2016. As of September 30, 2017, the warehouse lending operations had extended warehouse line commitments to non-affiliated customers totaling \$159.0 million as compared to \$175.5 million at December 31, 2016. By leveraging our re-warehousing division, our strategy is to increase the capture rate of our approved correspondent sellers business as well as expand our active customer base to include new customers seeking warehouse lines.

For the third quarter of 2017, real estate services fees were \$1.4 million as compared to \$1.5 million in the second quarter of 2017 and \$2.7 million in the third quarter of 2016. Since most of our real estate services business is generated from our long-term mortgage portfolio, as the long-term mortgage portfolio continues to decline, we expect real estate services and the related revenues to decline.

In our long-term mortgage portfolio, the residual interests generated cash flows of \$2.7 million in the third quarter of 2017 as compared to \$3.1 million in the second quarter of 2017 and \$1.6 million in the third quarter of 2016. The estimated fair value of the net residual interests decreased \$2.5 million in the third quarter of 2017 to \$17.4 million at September 30, 2017, as a result of residual cash flows received partially offset by an improvement in performance from certain trusts.

For additional information regarding the long-term mortgage portfolio refer to Financial Condition and Results of Operations below.

Liquidity and Capital Resources

During the nine months ended September 30, 2017, we funded our operations primarily from mortgage lending revenues and to a lesser extent real estate services fees and cash flows from our residual interests in securitizations. Mortgage lending revenues include gains on sale of loans, net, and other mortgage related income, and real estate services fees including portfolio loss mitigation fees primarily generated from our long-term mortgage portfolio. During the three and nine months ended September 30, 2017, we raised capital by issuing common stock as well as obtained MSR financing facilities, as further described below. Additionally, we funded mortgage loan originations using warehouse facilities which are repaid once the loan is sold. We may continue to manage our capital through the financing or sale of mortgage servicing rights. We may also seek to raise capital by issuing debt or equity, including offering shares through the "At-the-Market" offering (ATM) program we initiated in 2015.

On August 17, 2017, IMC (Borrower), issued a Line of Credit Promissory Note with a lender providing for a revolving line of credit of \$30.0 million (FHLMC Financing). The Borrower is able to borrow up to 55% of the fair market value of FHLMC pledged mortgage servicing rights. The Line of Credit has a term until May 31, 2018 and will automatically renew for subsequent one year periods unless the lender provides the Borrower 150 days' notice of its intention not to renew. Interest payments are payable monthly and accrue interest at the rate per annum equal to LIBOR plus 4.0% and the balance of the obligation may be prepaid at any time. The obligations under the FHLMC Financing are secured by FHLMC pledged mortgage servicing rights and Integrated Real Estate Services, Corp. is a guarantor. At September 30, 2017, \$5.0 million was outstanding under the FHLMC Financing.

On May 5, 2017, we entered into an exchange agreement pursuant to which we agreed to issue 412,264 shares of our common stock in exchange for trust preferred securities with an aggregate liquidation amount of \$8.5 million issued by Impac Capital Trust #4. Accrued and unpaid interest on the trust preferred securities was paid in cash in the aggregate amount of approximately \$14 thousand. The exchange was based on the carrying value of the trust preferred obligation which was \$5.6 million at March 31, 2017 and an agreed upon stock price of \$13.68 that determined a fixed number of shares to be issued in the exchange resulting in a discount to par of 34%. However, because the market value of the common stock was \$17.06 on the issuance date (measurement date), we recorded a \$1.3 million loss on extinguishment of debt during the three and nine months ended September 30, 2017. The appreciation in stock price from the agreement date to the issuance date of the common stock resulted in a loss on extinguishment of debt. The annual interest savings will amount to approximately \$400 thousand.

On April 18, 2017, we received \$56.0 million from the issuance of common stock in a registered direct offering (Offering) at a price of \$12.66 per share. In the Offering, we issued an aggregate of 4,423,381 shares of common stock.

Net proceeds from the Offering were approximately \$55.5 million after deducting the financial advisory fee and estimated aggregate offering expenses. We intend to use the net proceeds from the Offering for general corporate purposes, including general administrative expenses and working capital and capital expenditures, development costs, strategic investments or possible acquisitions, or repayment of debt.

In February 2017, we entered into a Loan and Security Agreement (Agreement) with a lender providing for a revolving loan commitment of up to \$40.0 million for a period of two years (FNMA Financing) to finance MSRs. We are able to borrow up to 55% of the fair market value of FNMA pledged servicing rights. Upon the two year anniversary of the Agreement, any amounts outstanding will automatically be converted into a term loan due and payable in full on the one year anniversary of the conversion date. Interest payments are payable monthly and accrue interest at the rate per annum equal to one-month LIBOR plus 4.0%. The balance of the obligation may be prepaid at any time. With the initial draw of \$35.1 million, a portion of the proceeds were used to pay off the Term Financing (approximately \$30.1 million) originally entered into in June 2015. At September 30, 2017, the outstanding balance of the FNMA Financing was \$20.1 million.

During the nine months ended September 30, 2017, we paid approximately \$16.2 million in contingent consideration payments related to the CCM acquisition for the fourth quarter of 2016, the first and second quarters of 2017 earn-out period. Additionally, the contingent consideration payment for the third quarter of 2017 is approximately \$4.7 million and is due in November 2017. These contingent consideration payments are based on the performance of the CCM division and over time the earn-out percentage declines. The fourth quarter 2016 earn-out percentage was 55% of the CCM division earnings, as defined. Beginning in 2017, the earn-out percentage decreased to 45% and terminates at the end of 2017.

Our results of operations and liquidity are materially affected by conditions in the markets for mortgages and mortgage-related assets, as well as the broader financial markets and the general economy. Concerns over economic recession, geopolitical issues, unemployment, the availability and cost of financing, the mortgage market and real estate market conditions contribute to increased volatility and diminished expectations for the economy and markets. Volatility and uncertainty in the marketplace may make it more difficult for us to obtain financing or raise capital on favorable terms or at all. Our operations and profitability may be adversely affected if we are unable to obtain cost-effective financing.

We believe that current cash balances, cash flows from our mortgage lending operations, the sale of mortgage servicing rights, real estate services fees generated from our long-term mortgage portfolio, and residual interest cash flows from our long-term mortgage portfolio are adequate for our current operating needs. We believe the mortgage and real estate services market is volatile, highly competitive and subject to increased regulation. Competition in mortgage lending comes primarily from mortgage bankers, commercial banks, credit unions and other finance companies which operate in our market area as well as throughout the United States. We compete for loans principally on the basis of the interest rates and loan fees we charge, the types of loans we originate and the quality of services we provide to borrowers, brokers and sellers. Additionally, performance of the long-term mortgage portfolio is subject to the current real estate market and economic conditions. Cash flows from our residual interests in securitizations are sensitive to delinquencies, defaults and credit losses associated with the securitized loans. Losses in excess of current estimates will reduce the residual interest cash receipts from our long-term mortgage portfolio.

While we continue to pay our obligations as they become due, the ability to continue to meet our current and long-term obligations is dependent upon many factors, particularly our ability to successfully operate our mortgage lending segment, real estate services segment and realizing cash flows from the long-term mortgage portfolio. Our future financial performance and profitability are dependent in large part upon the ability to expand our mortgage lending platform successfully.

Critical Accounting Policies

We define critical accounting policies as those that are important to the portrayal of our financial condition and results of operations. Our critical accounting policies require management to make difficult and complex judgments that rely on estimates about the effect of matters that are inherently uncertain due to the effect of changing market conditions and/or consumer behavior. In determining which accounting policies meet this definition, we considered our policies with respect to the valuation of our assets and liabilities and estimates and assumptions used in determining those

[Table of Contents](#)

valuations. We believe the most critical accounting issues that require the most complex and difficult judgments and that are particularly susceptible to significant change to our financial condition and results of operations include those issues included in Management's Discussion and Analysis of Results of Operations in IMH's report on Form 10-K for the year ended December 31, 2016. Such policies have not changed during 2017.

Financial Condition and Results of Operations

Financial Condition

As of September 30, 2017 compared to December 31, 2016

The following table shows the condensed consolidated balance sheets for the following periods:

	September 30, 2017	December 31, 2016	Increase (Decrease)	% Change
ASSETS				
Cash	\$ 34,815	\$ 40,096	\$ (5,281)	(13)%
Restricted cash	6,605	5,971	634	11
Mortgage loans held-for-sale	572,268	388,422	183,846	47
Finance receivables	60,912	62,937	(2,025)	(3)
Mortgage servicing rights	158,950	131,537	27,413	21
Securitized mortgage trust assets	3,769,231	4,033,290	(264,059)	(7)
Goodwill	104,938	104,938	—	—
Intangibles, net	22,631	25,778	(3,147)	(12)
Deferred tax asset, net	24,420	24,420	—	—
Other assets	60,607	46,345	14,262	31
Total assets	\$ 4,815,377	\$ 4,863,734	\$ (48,357)	(1)%
LIABILITIES & EQUITY				
Warehouse borrowings	\$ 591,583	\$ 420,573	\$ 171,010	41 %
MSR financings	25,133	—	25,133	n/a
Convertible notes	24,972	24,965	7	0
Contingent consideration	5,816	31,072	(25,256)	(81)
Long-term debt (Par value; \$62,000 and \$70,500)	44,561	47,207	(2,646)	(6)
Securitized mortgage trust liabilities	3,751,831	4,017,603	(265,772)	(7)
Repurchase reserve	4,980	5,408	(428)	(8)
Term financing, net	—	29,910	(29,910)	(100)
Other liabilities	57,048	55,956	1,092	2
Total liabilities	4,505,924	4,632,694	(126,770)	(3)
Total equity	309,453	231,040	78,413	34
Total liabilities and stockholders' equity	\$ 4,815,377	\$ 4,863,734	\$ (48,357)	(1)%
Book value per share	\$ 14.77	14.42	0.35	2 %

At September 30, 2017, cash decreased \$5.3 million from \$40.1 million at December 31, 2016. Cash balances decreased primarily due to repayment of the \$30.0 million term financing, \$16.2 million earn-out payments to CashCall Inc. based upon CCM earnings for the fourth quarter of 2016 and the first and second quarters of 2017, \$5.6 million purchase of mortgage servicing rights and a \$10.8 million increase in warehouse haircuts (difference between loan balance funded and amount advanced by warehouse lender) associated with the increase in mortgage loans held-for-sale (LHFS). Partially offsetting the decrease in cash was \$55.5 million in proceeds from common stock offering, \$25.1 million in net borrowings under the MSR financing facility and \$11.0 million in residual cash flows.

LHFS increased \$183.8 million to \$572.3 million at September 30, 2017 as compared to \$388.4 million at December 31, 2016. The increase was due to \$5.5 billion in originations during the first nine months of 2017 partially

[Table of Contents](#)

offset by \$5.3 billion in loan sales. As a normal course of our origination and sales cycle, loans held-for-sale at the end of any period are generally sold within one or two subsequent months.

Finance receivables decreased \$2.0 million to \$60.9 million at September 30, 2017 as compared to \$62.9 million at December 31, 2016. The decrease was primarily due to \$714.2 million in fundings offset by \$716.2 million in settlements during the nine months ended September 30, 2017.

MSRs increased \$27.4 million to \$159.0 million at September 30, 2017 as compared to \$131.5 million at December 31, 2016. The increase was due to servicing retained loan sales of \$4.7 billion in UPB as well as a purchase of approximately \$570.0 million in UPB of MSRs. Partially offsetting the increase was a bulk sale of NonQM MSRs totaling approximately \$155.9 million in UPB and a mark-to-market reduction in fair value of \$20.0 million. At September 30, 2017, we serviced \$15.7 billion in UPB for others as compared to \$12.4 billion at December 31, 2016.

Warehouse borrowings increased \$171.0 million to \$591.6 million at September 30, 2017 as compared to \$420.6 million at December 31, 2016. The increase was due to an increase in LHFS at September 30, 2017. We increased our total borrowing capacity to \$960.0 million from \$925.0 million at December 31, 2016.

In August and February 2017, we entered into separate Agreements with two lenders providing for MSR financing facilities of up to \$30.0 million and \$40.0 million. The \$30.0 million facility allows us to borrow up to 55% of the fair market value of FHLMC pledged mortgage servicing rights. The \$40.0 million facility allows us to borrow up to 55% of the fair market value of FNMA pledged mortgage servicing rights. At September 30, 2017, the balance outstanding on the FHLMC and FNMA facilities was \$5.0 million and \$20.1 million, respectively.

Long-term debt decreased \$2.6 million to \$44.6 million at September 30, 2017 as compared to \$47.2 million at December 31, 2016. The decrease was due to the exchange agreement entered into in May 2017, whereby we issued 412,264 shares of common stock in exchange for trust preferred securities with a fair value of \$5.6 million. Partially offsetting the decrease in long-term debt was a mark-to-market increase in fair value of \$2.7 million.

Book value per share increased to \$14.77 at September 30, 2017 as compared to \$14.42 at December 31, 2016. Book value per common share increased 10% to \$12.30 as of September 30, 2017, as compared to \$11.19 as of December 31, 2016 (inclusive of the remaining \$51.8 million of liquidation preference on our preferred stock).

The changes in total assets and liabilities, at fair market value, are primarily attributable to decreases in our trust assets and trust liabilities as summarized below.

	September 30, 2017	December 31, 2016	Increase (Decrease)	% Change
Securitized mortgage collateral	\$ 3,758,140	\$ 4,021,891	\$ (263,751)	(7)%
Other trust assets	11,091	11,399	(308)	(3)
Total trust assets	3,769,231	4,033,290	(264,059)	(7)
Securitized mortgage borrowings	\$ 3,751,831	\$ 4,017,603	\$ (265,772)	(7)%
Total trust liabilities	3,751,831	4,017,603	(265,772)	(7)
Residual interests in securitizations	\$ 17,400	\$ 15,687	\$ 1,713	11 %

Since the consolidated and unconsolidated securitization trusts are nonrecourse to us, trust assets and liabilities have been netted to present our interest in these trusts more simply, which are considered the residual interests in securitizations. For unconsolidated securitizations the residual interests represent the fair value of investment securities available-for-sale. For consolidated securitizations, the residual interests are represented by the fair value of securitized mortgage collateral and real estate owned, offset by the fair value of securitized mortgage borrowings and derivative liabilities. We receive cash flows from our residual interests in securitizations to the extent they are available after required distributions to bondholders and maintaining specified overcollateralization levels and other specified parameters (such as maximum delinquency and cumulative default) within the trusts. The estimated fair value of the residual interests, represented by the difference in the fair value of total trust assets and total trust liabilities, was \$17.4 million at September 30, 2017 as compared to \$15.7 million at December 31, 2016.

We update our collateral assumptions quarterly based on recent delinquency, default, prepayment and loss experience. Additionally, we update the forward interest rates and investor yield (discount rate) assumptions based on information derived from market participants. During the nine months ended September 30, 2017, actual losses were relatively flat and were inline with forecasted losses for the majority of trusts with residual value. Principal payments and liquidations of securitized mortgage collateral and securitized mortgage borrowings also contributed to the reduction in trust assets and liabilities. The increase in residual fair value at September 30, 2017 was the result of a decrease in loss assumptions as well as recoveries on certain multifamily trusts with residual value.

- The estimated fair value of securitized mortgage collateral decreased \$263.8 million during the nine months ended September 30, 2017, primarily due to reductions in principal from borrower payments and transfers of loans to Real Estate Owned (REO) for single-family and multi-family collateral. Additionally, other trust assets decreased \$0.3 million during the nine months ended September 30, 2017, primarily due to REO liquidations of \$24.2 million. Partially offsetting the decrease was an increase of \$15.4 million in REO from foreclosures and an \$8.5 million increase in the net realizable value (NRV) of REO.
- The estimated fair value of securitized mortgage borrowings decreased \$265.8 million during the nine months ended September 30, 2017, primarily due to reductions in principal balances from principal payments during the period for single-family and multi-family collateral as well as a decrease in loss assumptions.

Prior to 2008, we securitized mortgage loans by transferring originated and acquired residential single-family mortgage loans and multi-family commercial loans (the “transferred assets”) into nonrecourse bankruptcy remote trusts which in turn issued tranches of bonds to investors supported only by the cash flows of the transferred assets. Because the assets and liabilities in the securitizations are nonrecourse to us, the bondholders cannot look to us for repayment of their bonds in the event of a shortfall. These securitizations were structured to include interest rate derivatives. We retained the residual interest in each trust, and in most cases would perform the master servicing function. A trustee and sub-servicer, unrelated to us, were utilized for each securitization. Cash flows from the loans (the loan payments as well as liquidation of foreclosed real estate properties) collected by the loan sub-servicer are remitted to us, the master servicer. The master servicer remits payments to the trustee who remits payments to the bondholders (investors). The sub-servicer collects loan payments and performs loss mitigation activities for defaulted loans. These activities include foreclosing on properties securing defaulted loans, which results in REO.

To estimate fair value of the assets and liabilities within the securitization trusts each reporting period, management uses an industry standard valuation and analytical model that is updated monthly with current collateral, real estate, derivative, bond and cost (servicer, trustee, etc.) information for each securitization trust. We employ an internal process to validate the accuracy of the model as well as the data within this model. Forecasted assumptions sometimes referred to as “curves,” for defaults, loss severity, interest rates (LIBOR) and prepayments are inputted into the valuation model for each securitization trust. We hire third-party market participants to provide forecasted curves for the aforementioned assumptions for each of the securitizations. Before inputting this information into the model, management employs a process to qualitatively and quantitatively review the assumption curves for reasonableness using other information gathered from the mortgage and real estate market (*i.e.*, third party home price indices, published industry reports discussing regional mortgage and commercial loan performance and delinquency) as well as actual default and foreclosure information for each trust from the respective trustees.

We use the valuation model to generate the expected cash flows to be collected from the trust assets and the expected required bondholder distribution (trust liabilities). To the extent that the trusts are over collateralized, we may receive the excess interest as the holder of the residual interest. The information above provides us with the future expected cash flows for the securitized mortgage collateral, real estate owned, securitized mortgage borrowings, derivative assets/liabilities, and the residual interests.

To determine the discount rates to apply to these cash flows, we gather information from the bond pricing services and other market participants regarding estimated investor required yields for each bond tranche. Based on that information and the collateral type and vintage, we determine an acceptable range of expected yields an investor would require including an appropriate risk premium for each bond tranche. We use the blended yield of the bond tranches together with the residual interests to determine an appropriate yield for the securitized mortgage collateral in each securitization (after taking into consideration any derivatives in the securitization).

[Table of Contents](#)

The following table presents changes in the trust assets and trust liabilities for the nine months ended September 30, 2017:

	Level 3 Recurring Fair Value Measurement			TRUST LIABILITIES	
	Securitized mortgage collateral	NRV (1)	Total trust assets	Level 3 Recurring Fair Value Measurement	
		Real estate owned		Securitized mortgage borrowings	Net trust assets
Recorded book value at December 31, 2016	\$ 4,021,891	\$ 11,399	\$ 4,033,290	\$ (4,017,603)	\$ 15,687
Total gains/(losses) included in earnings:					
Interest income	39,564	—	39,564	—	39,564
Interest expense	—	—	—	(108,010)	(108,010)
Change in FV of net trust assets, excluding REO (2)	219,604	—	219,604	(221,510)	(1,906)
Gains from REO – not at FV but at NRV (2)	—	8,484	8,484	—	8,484
Total gains (losses) included in earnings	259,168	8,484	267,652	(329,520)	(61,868)
Transfers in and/or out of level 3	—	—	—	—	—
Purchases, issuances and settlements	(522,919)	(8,792)	(531,711)	595,292	63,581
Recorded book value at September 30, 2017	\$ 3,758,140	\$ 11,091	\$ 3,769,231	\$ (3,751,831)	\$ 17,400

(1) Accounted for at net realizable value.

(2) Represents change in fair value of net trust assets, including trust REO (losses) gains in the consolidated statements of operations for the nine months ended September 30, 2017.

Inclusive of gains from REO, total trust assets above reflect a net gain of \$228.1 million for the nine months ended September 30, 2017 as a result of an increase in fair value from securitized mortgage collateral of \$219.6 million and gains from REO of \$8.5 million. Net losses on trust liabilities were \$221.5 million from the increase in fair value of securitized mortgage borrowings. As a result, non-interest income—net trust assets totaled an increase of \$6.6 million for the nine months ended September 30, 2017.

The table below reflects the net trust assets as a percentage of total trust assets (residual interests in securitizations):

	September 30, 2017	December 31, 2016
Net trust assets	\$ 17,400	\$ 15,687
Total trust assets	3,769,231	4,033,290
Net trust assets as a percentage of total trust assets	0.46 %	0.39 %

For the nine months ended September 30, 2017, the estimated fair value of the net trust assets increased as a percentage of total trust assets. The increase was primarily due to an increase in projected future cash flows due to a decrease in loss assumptions in the 2006 multi-family vintage.

Since the consolidated and unconsolidated securitization trusts are nonrecourse to us, our economic risk is limited to our residual interests in these securitization trusts. Therefore, in the following table we have netted trust assets and trust liabilities to present these residual interests more simply. Our residual interests in securitizations are segregated between our single-family (SF) residential and multi-family (MF) residential portfolios and are represented by the difference between trust assets and trust liabilities.

[Table of Contents](#)

The following tables present the estimated fair value of our residual interests, including investment securities available for sale, by securitization vintage year and other related assumptions used to derive these values at September 30, 2017 and December 31, 2016:

Origination Year	Estimated Fair Value of Residual Interests by Vintage Year at September 30, 2017			Estimated Fair Value of Residual Interests by Vintage Year at December 31, 2016		
	SF	MF	Total	SF	MF	Total
2002-2003 (1)	\$ 8,412	\$ 699	\$ 9,111	\$ 8,402	\$ 921	\$ 9,323
2004	1,267	579	1,846	1,267	653	1,920
2005	23	42	65	—	—	—
2006	—	6,378	6,378	—	4,444	4,444
Total	\$ 9,702	\$ 7,698	\$ 17,400	\$ 9,669	\$ 6,018	\$ 15,687
Weighted avg. prepayment rate	6.8 %	9.2 %	7.0 %	6.3 %	10.1 %	6.6 %
Weighted avg. discount rate	16.3 %	18.6 %	17.3 %	16.3 %	17.9 %	16.9 %

(1) 2002-2003 vintage year includes CMO 2007-A, since the majority of the mortgages collateralized in this securitization were originated during this period.

We utilize a number of assumptions to value securitized mortgage collateral, securitized mortgage borrowings and residual interests. These assumptions include estimated collateral default rates and loss severities (credit losses), collateral prepayment rates, forward interest rates and investor yields (discount rates). We use the same collateral assumptions for securitized mortgage collateral and securitized mortgage borrowings as the collateral assumptions determine collateral cash flows which are used to pay interest and principal for securitized mortgage borrowings and excess spread, if any, to the residual interests. However, we use different investor yield (discount rate) assumptions for securitized mortgage collateral and securitized mortgage borrowings and the discount rate used for residual interests based on underlying collateral characteristics, vintage year, assumed risk and market participant assumptions. The increase in the estimated fair value of the 2006 multi-family residual interests was due to a reduction in future loss assumptions and recoveries within certain trusts.

The table below reflects the estimated future credit losses and investor yield requirements for trust assets by product (SF and MF) and securitization vintage at September 30, 2017:

	Estimated Future Losses (1)		Investor Yield Requirement (2)	
	SF	MF	SF	MF
2002-2003	5 %	* (3)	6 %	7 %
2004	9	* (3)	5	5
2005	11	* %	5	4
2006	12	1	6	4
2007	9	* (3)	7	3

(1) Estimated future losses derived by dividing future projected losses by UPB at September 30, 2017.

(2) Investor yield requirements represent our estimate of the yield third-party market participants would require to price our trust assets and liabilities given our prepayment, credit loss and forward interest rate assumptions.

(3) Represents less than 1%.

Despite the increase in housing prices through September 30, 2017, housing prices in many parts of the country are still at levels which have significantly reduced or eliminated equity for loans originated after 2003. Future loss estimates are significantly higher for mortgage loans included in securitization vintages after 2005 which reflect severe home price deterioration and defaults experienced with mortgages originated during these periods.

Long-Term Mortgage Portfolio Credit Quality

We use the Mortgage Bankers Association (MBA) method to define delinquency as a contractually required payment being 30 or more days past due. We measure delinquencies from the date of the last payment due date in which a payment was received. Delinquencies for loans 60 days delinquent or greater, foreclosures and delinquent bankruptcies were \$834.0 million or 18.7% of the long-term mortgage portfolio as of September 30, 2017 as compared to \$1.0 billion or 20.0% as of December 31, 2016.

The following table summarizes the gross UPB of loans in our mortgage portfolio, included in securitized mortgage collateral, that were 60 or more days delinquent (utilizing the MBA method) as of the periods indicated:

Securitized mortgage collateral	September 30, 2017	Total Collateral	December 31, 2016	Total Collateral
60 - 89 days delinquent	\$ 102,044	2.3 %	\$ 140,567	2.8 %
90 or more days delinquent	349,684	7.8	417,947	8.2
Foreclosures (1)	176,757	4.0	224,633	4.4
Delinquent bankruptcies (2)	205,500	4.6	232,249	4.6
Total 60 or more days delinquent	\$ 833,985	18.7	\$ 1,015,396	20.0
Total collateral	\$ 4,454,670	100.0	\$ 5,078,500	100.0

- (1) Represents properties in the process of foreclosure.
(2) Represents bankruptcies that are 30 days or more delinquent.

The following table summarizes the gross securitized mortgage collateral and REO at NRV, that were non-performing as of the dates indicated (excludes 60-89 days delinquent):

	September 30, 2017	Total Collateral %	December 31, 2016	Total Collateral %
90 or more days delinquent, foreclosures and delinquent bankruptcies	\$ 731,941	16.4 %	\$ 874,829	17.2 %
Real estate owned	11,091	0.2	11,399	0.2
Total non-performing assets	\$ 743,032	16.6	\$ 886,228	17.4

Non-performing assets consist of non-performing loans (mortgages that are 90 or more days delinquent, including loans in foreclosure and delinquent bankruptcies) plus REO. It is our policy to place a mortgage on nonaccrual status when it becomes 90 days delinquent and to reverse from revenue any accrued interest, except for interest income on securitized mortgage collateral when the scheduled payment is received from the servicer. The servicers are required to advance principal and interest on loans within the securitization trusts to the extent the advances are considered recoverable. IFC, a subsidiary of IMH and master servicer, may be required to advance funds, or in most cases cause the loan servicers to advance funds, to cover principal and interest payments not received from borrowers depending on the status of their mortgages. As of September 30, 2017, non-performing assets (UPB of loans 90 or more days delinquent, foreclosures and delinquent bankruptcies plus REO) as a percentage of the total collateral was 16.6%. At December 31, 2016, non-performing assets to total collateral was 17.4%. Non-performing assets decreased by approximately \$143.2 million at September 30, 2017 as compared to December 31, 2016. At September 30, 2017, the estimated fair value of non-performing assets (representing the fair value of loans 90 or more days delinquent, foreclosures and delinquent bankruptcies plus REO) was \$245.8 million or 5.1% of total assets. At December 31, 2016, the estimated fair value of non-performing assets was \$263.6 million or 5.4% of total assets.

REO, which consists of residential real estate acquired in satisfaction of loans, is carried at the lower of cost or net realizable value less estimated selling costs. Adjustments to the loan carrying value required at the time of foreclosure are included in the change in the fair value of net trust assets. Changes in our estimates of net realizable value subsequent to the time of foreclosure and through the time of ultimate disposition are recorded as change in fair value of net trust assets including trust REO gains (losses) in the consolidated statements of operations.

[Table of Contents](#)

For the three and nine months ended September 30, 2017, we recorded an increase in net realizable value of REO in the amount of \$2.7 million and \$8.5 million, respectively, compared to a decrease of \$1.4 million and \$6.0 million for the comparable 2016 period. Increases and write-downs of the net realizable value reflect increases or declines in value of the REO subsequent to foreclosure date, but prior to the date of sale.

The following table presents the balances of REO:

	<u>September 30,</u> <u>2017</u>	<u>December 31,</u> <u>2016</u>
REO	\$ 17,009	\$ 25,802
Impairment (1)	(5,918)	(14,403)
Total	<u>\$ 11,091</u>	<u>\$ 11,399</u>

(1) Impairment represents the cumulative write-downs of net realizable value subsequent to foreclosure.

In calculating the cash flows to assess the fair value of the securitized mortgage collateral, we estimate the future losses embedded in our loan portfolio. In evaluating the adequacy of these losses, management takes many factors into consideration. For instance, a detailed analysis of historical loan performance data is accumulated and reviewed. This data is analyzed for loss performance and prepayment performance by product type, origination year and securitization issuance. The data is also broken down by collection status. Our estimate of losses for these loans is developed by estimating both the rate of default of the loans and the amount of loss severity in the event of default. The rate of default is assigned to the loans based on their attributes (*e.g.*, original loan-to-value, borrower credit score, documentation type, geographic location, etc.) and collection status. The rate of default is based on analysis of migration of loans from each aging category. The loss severity is determined by estimating the net proceeds from the ultimate sale of the foreclosed property. The results of that analysis are then applied to the current mortgage portfolio and an estimate is created. We believe that pooling of mortgages with similar characteristics is an appropriate methodology in which to evaluate the future loan losses.

Management recognizes that there are qualitative factors that must be taken into consideration when evaluating and measuring losses in the loan portfolios. These items include, but are not limited to, economic indicators that may affect the borrower's ability to pay, changes in value of collateral, political factors, employment and market conditions, competitor's performance, market perception, historical losses, and industry statistics. The assessment for losses is based on delinquency trends and prior loss experience and management's judgment and assumptions regarding various matters, including general economic conditions and loan portfolio composition. Management continually evaluates these assumptions and various relevant factors affecting credit quality and inherent losses.

Results of Operations

For the Three Months Ended September 30, 2017 compared to the Three Months Ended September 30, 2016

	<u>For the Three Months Ended September 30,</u>			
	<u>2017</u>	<u>2016</u>	<u>Increase (Decrease)</u>	<u>% Change</u>
Revenues	\$ 42,076	\$ 103,993	\$ (61,917)	(60)%
Expenses (1)	(37,560)	(81,359)	43,799	54
Net interest income	1,546	1,304	242	19
Loss on extinguishment of debt	—	—	—	n/a
Change in fair value of long-term debt	104	(8,641)	8,745	(101)
Change in fair value of net trust assets, including trust REO gains (losses)	(1,745)	1,071	(2,816)	(263)
Income tax (expense) benefit	(2,104)	130	(2,234)	1718
Net earnings	<u>\$ 2,317</u>	<u>\$ 16,498</u>	<u>\$ (14,181)</u>	<u>(86)</u>
Earnings per share available to common stockholders—basic	<u>\$ 0.11</u>	<u>\$ 1.28</u>	<u>\$ (1.17)</u>	<u>(91)%</u>
Earnings per share available to common stockholders—diluted	<u>\$ 0.11</u>	<u>\$ 1.18</u>	<u>\$ (1.07)</u>	<u>(91)%</u>

(1) Includes changes in contingent consideration liability resulting in income of \$4.8 million and an expense of \$23.2 million for the three months ended September 30, 2017 and 2016, respectively.

For the Nine Months Ended September 30, 2017 compared to the Nine Months Ended September 30, 2016

	For the Nine Months Ended September 30,			
	2017	2016	Increase (Decrease)	% Change
Revenues	\$ 127,051	\$ 220,506	\$ (93,455)	(42)%
Expenses (1)	(115,838)	(187,408)	71,570	38
Net interest income (expense)	3,090	2,036	1,054	52
Loss on extinguishment of debt	(1,265)	—	(1,265)	n/a
Change in fair value of long-term debt	(2,657)	(7,286)	4,629	(64)
Change in fair value of net trust assets, including trust REO gains (losses)	6,578	2,609	3,969	152
Income tax expense	(3,575)	(728)	(2,847)	(391)
Net earnings	\$ 13,384	\$ 29,729	\$ (16,345)	(55)
Earnings per share available to common stockholders—basic	\$ 0.71	\$ 2.43	\$ (1.72)	(71)%
Earnings per share available to common stockholders—diluted	\$ 0.71	\$ 2.27	\$ (1.56)	(69)%

(1) Includes changes in contingent consideration liability resulting in income of \$11.1 million and an expense of \$34.6 million for the nine months ended September 30, 2017 and 2016, respectively.

Revenues

	For the Three Months Ended September 30,			
	2017	2016	Increase (Decrease)	% Change
Gain on sale of loans, net	\$ 42,476	\$ 113,158	\$ (70,682)	(62)%
Real estate services fees, net	1,355	2,678	(1,323)	(49)
Servicing fees, net	8,492	3,789	4,703	124
Loss on mortgage servicing rights, net	(10,513)	(15,857)	5,344	34
Other revenues	266	225	41	18
Total revenues	\$ 42,076	\$ 103,993	\$ (61,917)	(60)%

Gain on sale of loans, net. For the three months ended September 30, 2017, gain on sale of loans, net were \$42.5 million compared to \$113.2 million in the comparable 2016 period. The \$70.7 million decrease is primarily due to a \$52.8 million decrease in premiums from the sale of mortgage loans, a \$23.0 million decrease in premiums from servicing retained loan sales, a \$6.6 million decrease in mark-to-market gains on LHFS, a \$3.5 million decrease in realized and unrealized net gains on derivative financial instruments and a \$1.8 million increase in provision for repurchases, partially offset by a \$17.2 million decrease in direct loan origination expenses.

The overall decrease in gain on sale of loans, net was primarily due to a 51% decrease in volume as well as a decrease in gain on sale margins. For the three months ended September 30, 2017, we originated and sold \$2.1 billion and \$2.1 billion of loans, respectively, as compared to \$4.2 billion and \$4.1 billion of loans originated and sold, respectively, during the same period in 2016. Margins decreased to approximately 204 bps for the three months ended September 30, 2017 as compared to 268 bps for the same period in 2016 due to margin compression across all three channels as a result of the increase in interest rates as compared to the third quarter of 2016 as well as an increase in competition for volume.

Real estate services fees, net. For the three months ended September 30, 2017, real estate services fees, net were \$1.4 million compared to \$2.7 million in the comparable 2016 period. The \$1.3 million decrease was primarily the result of a decrease in transactions related to the decline in the number of loans and the UPB of the long-term mortgage portfolio as compared to 2016.

Servicing fees, net. For the three months ended September 30, 2017, servicing fees, net was \$8.5 million compared to \$3.8 million in the comparable 2016 period. The increase in servicing fees, net was the result of the servicing portfolio increasing 81% to an average balance of \$15.4 billion for the three months ended September 30, 2017

[Table of Contents](#)

as compared to an average balance of \$8.5 billion for the three months ended September 30, 2016. The increase in the average balance of the servicing portfolio is a result of our efforts during the past year to retain servicing with fewer bulk sales of MSRs. We had \$1.9 billion in servicing retained loan sales during the three months ended September 30, 2017 with no bulk sales of MSRs.

Loss on mortgage servicing rights, net. For the three months ended September 30, 2017, loss on MSRs, net was \$10.5 million compared to \$15.9 million in the comparable 2016 period. For the three months ended September 30, 2017, we recorded an \$11.2 million loss from a change in fair value of MSRs primarily the result of mark-to-market changes related to amortization as well as an increase in prepayment speeds. During the quarter, we had an \$8 thousand loss on sale of mortgage servicing rights related to refunds of premiums to investors for loan payoffs associated with sales of servicing rights in previous periods. Partially offsetting the loss was \$672 thousand in realized and unrealized gains from hedging instruments related to MSRs.

	For the Nine Months Ended September 30,			
	2017	2016	Increase (Decrease)	% Change
Gain on sale of loans, net	\$ 116,602	\$ 245,849	\$ (129,247)	(53)%
Real estate services fees, net	4,492	6,773	(2,281)	(34)
Servicing fees, net	23,575	8,680	14,895	172
Loss on mortgage servicing rights, net	(18,159)	(41,249)	23,090	56
Other revenues	541	453	88	19
Total revenues	<u>\$ 127,051</u>	<u>\$ 220,506</u>	<u>\$ (93,455)</u>	(42)

Gain on sale of loans, net. For the nine months ended September 30, 2017, gain on sale of loans, net were \$116.6 million compared to \$245.8 million in the comparable 2016 period. The \$129.2 million decrease is primarily due to a \$108.3 million decrease in premiums from the sale of mortgage loans, a \$49.1 million decrease in premiums from servicing retained loan sales and an \$11.3 million decrease in mark-to-market gains on LHFS, partially offset by a \$39.6 million decrease in direct loan origination expenses, \$149 thousand decrease in realized and unrealized net losses on derivative financial instruments and a \$586 thousand decrease in provision for repurchases.

The overall decrease in gain on sale of loans, net was primarily due to a 44% decrease in volumes as well as a decrease in gain on sale margins. For the nine months ended September 30, 2017 we originated and sold \$5.5 billion and \$5.3 billion of loans, respectively, as compared to \$9.8 billion and \$9.3 billion of loans originated and sold, respectively, during the same period in 2016. Margins decreased to approximately 214 bps for the nine months ended September 30, 2017 as compared to 251 bps for the same period in 2016 due to margin compression across all three channels as a result of the increase in interest rates as compared to the first nine months of 2016 as well as an increase in competition for volume.

Real estate services fees, net. For the nine months ended September 30, 2017, real estate services fees, net were \$4.5 million compared to \$6.8 million in the comparable 2016 period. The \$2.3 million decrease was primarily the result of a decrease in transactions related to the decline in the number of loans and the UPB of the long-term mortgage portfolio as compared to 2016.

Servicing fees, net. For the nine months ended September 30, 2017, servicing fees, net was \$23.6 million compared to \$8.7 million in the comparable 2016 period. The increase in servicing fees, net was the result of the servicing portfolio increasing 122% to an average balance of \$14.1 billion for the nine months ended September 30, 2017 as compared to an average balance of \$6.4 billion for the nine months ended September 30, 2016. The increase in the average balance of the servicing portfolio is a result of our efforts during the past year to retain servicing with fewer bulk sales of MSRs. We had \$4.7 billion in servicing retained loan sales during the nine months ended September 30, 2017. Partially offsetting the increase was a bulk sale of NonQM MSRs totaling approximately \$155.9 million in UPB.

[Table of Contents](#)

Loss on mortgage servicing rights, net. For the nine months ended September 30, 2017, loss on MSRs, net was \$18.2 million compared to \$41.2 million in the comparable 2016 period. For the nine months ended September 30, 2017, we recorded a \$20.0 million loss from a change in fair value of MSRs primarily the result of mark-to-market changes related to amortization as well as an increase in prepayment speeds. During the nine months ended September 30, 2017, we had a \$90 thousand loss on sale of mortgage servicing rights related to refunds of premiums to investors for loan payoffs partially offset by recoveries of previously written off holdbacks associated with sales of servicing rights in previous periods. Partially offsetting the loss was a \$2.0 million increase in realized and unrealized gains from hedging instruments related to MSRs.

Expenses

	For the Three Months Ended September 30,			
	2017	2016	Increase (Decrease)	% Change
Personnel expense	\$ 23,062	\$ 38,467	\$ (15,405)	(40)%
Business promotion	10,403	10,350	53	1
General, administrative and other	8,497	7,736	761	10
Accretion of contingent consideration	396	1,591	(1,195)	(75)
Change in fair value of contingent consideration	(4,798)	23,215	(28,013)	(121)
Total expenses	<u>\$ 37,560</u>	<u>\$ 81,359</u>	<u>\$ (43,799)</u>	(54)%

Total expenses were \$37.6 million for the three months ended September 30, 2017, compared to \$81.4 million for the comparable period of 2016. Personnel expense decreased \$15.4 million to \$23.1 million for the three months ended September 30, 2017. The decrease is primarily related to a reduction in commission expense due to a decrease in loan originations as well as staff reductions made in the first quarter of 2017. As a result of the staff reductions in the first quarter of 2017, average headcount decreased 24% for the third quarter of 2017 as compared to the same period in 2016.

Business promotion was flat at \$10.4 million for the three months ended September 30, 2017 and 2016. Our centralized call center purchases leads and promotes its business through radio and television advertisements. During the third quarter of 2017, business promotion was relatively flat as compared to 2016 with continued efforts to increase NonQM and purchase money production with the reduction in refinance activity as a result of the increase in interest rates as compared to the third quarter of 2016.

General, administrative and other expenses increased to \$8.5 million for the three months ended September 30, 2017, compared to \$7.7 million for the same period in 2016. The increase was primarily related to a \$1.8 million increase in legal and professional fees associated with defending litigation, as discussed in Item 3 of the 2016 10-K and in Item 1 of Part II within this 10-Q. Partially offsetting the increase was an \$534 thousand decrease in other general and administrative expenses, a \$294 thousand decrease in data processing and a \$187 thousand decrease in premises and equipment expense.

As part of the acquisition of CCM, we record accretion of the contingent consideration liability from the close of the transaction in March 2015 through the end of the earn-out period in December 2017, which increases the contingent consideration liability. The estimated contingent consideration liability is based on discounted cash flows which represent the time value of money of the liability during the earn-out period. In the third quarter of 2017, accretion increased the contingent consideration liability by \$396 thousand as compared to \$1.6 million during the third quarter of 2016. The decrease in accretion is due to the reduction of forecasted pre-tax earnings of CCM as a result of updated assumptions as well as a reduction in the estimated earn-out percentage as compared to 2016. The accretion will continue to be a charge against earnings in future quarters until the end of the earn-out period in December 2017.

We recorded a \$4.8 million change in fair value associated with a reduction in the contingent consideration liability for the third quarter of 2017 related to updated assumptions including current market conditions. The change in fair value of contingent consideration was primarily related to expected margin compression as well as a reduction in

[Table of Contents](#)

origination volume over the remaining earn-out period which ends in December 2017. The fair value of contingent consideration may change from quarter to quarter based upon actual experience and updated assumptions used to forecast pre-tax earnings for CCM. The decrease in the contingent consideration liability resulted in an increase in earnings of \$4.8 million in the third quarter of 2017.

	For the Nine Months Ended September 30,			
	2017	2016	Increase (Decrease)	% Change
Personnel expense	\$ 69,353	\$ 93,025	\$ (23,672)	(25)%
Business promotion	30,744	30,828	(84)	(0)
General, administrative and other	24,845	23,742	1,103	5
Accretion of contingent consideration	1,948	5,244	(3,296)	(63)
Change in fair value of contingent consideration	(11,052)	34,569	(45,621)	(132)
Total expenses	<u>\$ 115,838</u>	<u>\$ 187,408</u>	<u>\$ (71,570)</u>	(38)

Total expenses were \$115.8 million for the nine months ended September 30, 2017, compared to \$187.4 million for the comparable period of 2016. Personnel expense decreased \$23.7 million to \$69.4 million for the nine months ended September 30, 2017. The decrease is primarily related to a reduction in commission expense due to a decrease in loan originations as well as staff reductions made in the first quarter of 2017. With the decline in origination volumes in the first quarter of 2017 we made staff reductions, of which the full impact of the reductions were not reflected until the second quarter. As a result, average headcount decreased 13% for the nine months ended September 30, 2017 as compared to the same period in 2016.

Business promotion was \$30.7 million for the nine months ended September 30, 2017, compared to \$30.8 million for the comparable period of 2016. Our centralized call center purchases leads and promotes its business through radio and television advertisements. During the first nine months of 2017, business promotion was flat due to efforts to increase NonQM and purchase money production with the reduction in refinance activity as a result of the increase in interest rates as compared to the first nine months of 2016.

General, administrative and other expenses increased to \$24.8 million for the nine months ended September 30, 2017, compared to \$23.7 million for the same period in 2016. The increase was primarily related to a \$2.3 million increase in legal and professional fees associated with defending litigation, as discussed in Item 3 of the 2016 10-K and in Item 1 of Part II within this 10-Q and a \$155 thousand increase in occupancy expense. Partially offsetting the increase was a \$707 thousand decrease in other general and administrative expenses, a \$462 thousand decrease in premises and equipment and a \$215 thousand decrease in data processing expense.

As part of the acquisition of CCM, we record accretion of the contingent consideration liability from the close of the transaction in March 2015 through the end of the earn-out period in December 2017, which increases the contingent consideration liability. The estimated contingent consideration liability is based on discounted cash flows which represent the time value of money of the liability during the earn-out period. In the first nine months of 2017, accretion increased the contingent consideration liability by \$1.9 million as compared to \$5.2 million during the first nine months of 2016. The decrease in accretion is due to the reduction of forecasted pre-tax earnings of CCM as a result of updated assumptions as well as a reduction in the estimated earn-out percentage as compared to 2016. The accretion will continue to be a charge against earnings in future quarters until the end of the earn-out period in December 2017.

We recorded an \$11.1 million change in fair value associated with a reduction in the contingent consideration liability for the nine months ended September 30, 2017 related to updated assumptions including current market conditions. The change in fair value of contingent consideration was primarily related to expected margin compression as well as a reduction in volume over the remaining earn-out period which ends in December 2017. The fair value of contingent consideration may change from quarter to quarter based upon actual experience and updated assumptions used to forecast pre-tax earnings for CCM. The decrease in the contingent consideration liability resulted in an increase in earnings of \$11.1 million for the nine months ended September 30, 2017.

Net Interest Income (Expense)

We earn net interest income primarily from mortgage assets, which include securitized mortgage collateral, loans held-for-sale and finance receivables, or collectively, "mortgage assets," and, to a lesser extent, interest income earned on cash and cash equivalents. Interest expense is primarily interest paid on borrowings secured by mortgage assets, which include securitized mortgage borrowings and warehouse borrowings and to a lesser extent, interest expense paid on long-term debt, Convertible Notes, MSR Financing and Term Financing. Interest income and interest expense during the period primarily represents the effective yield, based on the fair value of the trust assets and liabilities.

The following tables summarize average balance, interest and weighted average yield on interest-earning assets and interest-bearing liabilities, for the periods indicated. Cash receipts and payments on derivative instruments hedging interest rate risk related to our securitized mortgage borrowings are not included in the results below. These cash receipts and payments are included as a component of the change in fair value of net trust assets.

	For the Three Months Ended September 30,					
	2017			2016		
	Average Balance	Interest	Yield	Average Balance	Interest	Yield
ASSETS						
Securitized mortgage collateral	\$ 3,767,162	\$ 51,606	5.48 %	\$ 4,223,226	\$ 59,616	5.65 %
Mortgage loans held-for-sale	452,390	5,465	4.83	494,918	4,606	3.72
Finance receivables	50,034	745	5.96	53,868	700	5.20
Other	33,733	38	0.45	15,401	10	0.26
Total interest-earning assets	<u>\$ 4,303,319</u>	<u>\$ 57,854</u>	5.38	<u>\$ 4,787,413</u>	<u>\$ 64,932</u>	5.43
LIABILITIES						
Securitized mortgage borrowings	\$ 3,759,675	\$ 49,629	5.28	\$ 4,219,975	\$ 57,043	5.41 %
Warehouse borrowings (1)	490,118	4,948	4.04	537,084	4,222	3.14
MSR financing facilities	13,014	192	5.90	—	—	—
Long-term debt	44,548	1,059	9.51	35,412	1,078	12.18
Convertible notes	24,970	471	7.55	24,963	469	7.52
Term financing	—	—	—	29,813	806	10.81
Other	390	9	9.23	755	10	5.30
Total interest-bearing liabilities	<u>\$ 4,332,715</u>	<u>\$ 56,308</u>	5.20	<u>\$ 4,848,002</u>	<u>\$ 63,628</u>	5.25
Net Interest Spread (2)		<u>\$ 1,546</u>	0.18 %		<u>\$ 1,304</u>	0.18 %
Net Interest Margin (3)			0.14 %			0.11 %

- (1) Warehouse borrowings include the borrowings from mortgage loans held-for-sale and finance receivables.
- (2) Net interest spread is calculated by subtracting the weighted average yield on interest-bearing liabilities from the weighted average yield on interest-earning assets.
- (3) Net interest margin is calculated by dividing net interest spread by total average interest-earning assets.

Net interest spread increased \$242 thousand for the three months ended September 30, 2017 primarily attributable to an increase in the net interest spread between loans held-for-sale and finance receivables and their related warehouse borrowings and a decrease in interest expense related to the payoff of the Term Financing. Partially offsetting the increase in net spread was a decrease in the net interest spread on the securitized mortgage collateral and securitized mortgage borrowings as well as an increase in interest expense as a result of the MSR financing facility. As a result, the net interest margin increased to 0.14% for the three months ended September 30, 2017 from 0.11% for the three months ended September 30, 2016.

During the quarter ended September 30, 2017, the yield on interest-earning assets decreased to 5.38% from 5.43% in the comparable 2016 period. The yield on interest-bearing liabilities decreased to 5.20% for the three months ended September 30, 2017 from 5.25% for the comparable 2016 period. In connection with the fair value accounting for securitized mortgage collateral and borrowings and long-term debt, interest income and interest expense is recognized using effective yields based on estimated fair values for these instruments. The decrease in yield for securitized

[Table of Contents](#)

mortgage collateral and securitized mortgage borrowings is primarily related to increased prices on mortgage-backed bonds which resulted in a decrease in yield as compared to the previous period.

	For the Nine Months Ended September 30,					
	2017			2016		
	Average Balance	Interest	Yield	Average Balance	Interest	Yield
ASSETS						
Securitized mortgage collateral	\$ 3,864,888	\$ 165,260	5.70 %	\$ 4,346,482	\$ 188,707	5.79 %
Mortgage loans held-for-sale	363,713	12,923	4.74	397,565	11,325	3.80
Finance receivables	38,118	1,695	5.93	37,302	1,502	5.37
Other	37,063	133	0.48	21,028	27	0.17
Total interest-earning assets	<u>\$ 4,303,782</u>	<u>\$ 180,011</u>	5.58	<u>\$ 4,802,377</u>	<u>\$ 201,561</u>	5.60
LIABILITIES						
Securitized mortgage borrowings	\$ 3,857,405	\$ 159,115	5.50 %	\$ 4,346,741	\$ 181,362	5.56 %
Warehouse borrowings (1)	392,108	11,896	4.05	425,882	10,701	3.35
MSR financing facilities	16,579	674	5.42	—	—	—
Long-term debt	46,587	3,393	9.71	33,716	3,088	12.21
Convertible notes	24,968	1,413	7.55	24,961	2,050	10.95
Term financing	4,490	408	12.12	29,792	2,300	10.29
Other	474	22	6.19	543	24	5.89
Total interest-bearing liabilities	<u>\$ 4,342,611</u>	<u>\$ 176,921</u>	5.43	<u>\$ 4,861,635</u>	<u>\$ 199,525</u>	5.47
Net Interest Spread (2)		\$ 3,090	0.15 %		\$ 2,036	0.13 %
Net Interest Margin (3)			0.10 %			0.06 %

- (1) Warehouse borrowings include the borrowings from mortgage loans held-for-sale and finance receivables.
- (2) Net interest spread is calculated by subtracting the weighted average yield on interest-bearing liabilities from the weighted average yield on interest-earning assets.
- (3) Net interest margin is calculated by dividing net interest spread by total average interest-earning assets.

Net interest spread increased \$1.1 million for the nine months ended September 30, 2017 primarily attributable to an increase in the net interest spread between loans held-for-sale and finance receivables and their related warehouse borrowings, a decrease in interest expense from the conversion of the Convertible Notes in January 2016 and a decrease in interest expense related to the payoff of the Term Financing. Offsetting the increase in net spread was a decrease in the net interest spread on the securitized mortgage collateral and securitized mortgage borrowings, an increase in the interest expense on the long-term debt as well as an increase in interest expense as a result of the MSR financing facilities. As a result, the net interest margin increased to 0.10% for the nine months ended September 30, 2017 from 0.06% for the nine months ended September 30, 2016.

During the nine months ended September 30, 2017, the yield on interest-earning assets decreased to 5.58% from 5.60% in the comparable 2016 period. The yield on interest-bearing liabilities decreased to 5.43% for the nine months ended September 30, 2017 from 5.47% for the comparable 2016 period. In connection with the fair value accounting for securitized mortgage collateral and borrowings and long-term debt, interest income and interest expense is recognized using effective yields based on estimated fair values for these instruments. The decrease in yield for securitized mortgage collateral and securitized mortgage borrowings is primarily related to increased prices on mortgage-backed bonds which resulted in a decrease in yield as compared to the previous period.

Loss on extinguishment of debt.

We recorded a \$1.3 million loss on extinguishment of debt during the nine months ended September 30, 2017. In May 2017, we exchanged 412,264 shares of common stock for the remaining trust preferred securities which had an aggregate liquidation amount of \$8.5 million. The value of the shares on the issuance date exceeded the carrying value of debt by \$1.3 million.

Change in the fair value of long-term debt.

Long-term debt (consisting of trust preferred securities and junior subordinated notes) is measured based upon an internal analysis, which considers our own credit risk and discounted cash flow analyses. Improvements in our financial results and financial condition in the future could result in additional increases in the estimated fair value of the long-term debt, while deterioration in financial results and financial condition could result in a decrease in the estimated fair value of the long-term debt.

Change in the fair value of long-term debt resulted in income of \$104 thousand and an expense of \$2.7 million for the three and nine months ended September 30, 2017, compared to an expense of \$8.6 million and \$7.3 million for the three and nine months ended September 30, 2016. The decrease in the estimated fair value of long-term debt in the third quarter of 2017 was the result of a slight decrease in the forward LIBOR curve. For the nine months ended September 30, 2017, the estimated fair value of long-term debt increased primarily due to a decrease in the discount rate attributable to an improvement in our credit risk profile, financial condition as well as an increase in LIBOR during 2017.

Change in fair value of net trust assets, including trust REO (losses) gains

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2017	2016	2017	2016
Change in fair value of net trust assets, excluding REO	\$ (4,479)	\$ 2,511	\$ (1,906)	\$ 8,580
Gains (losses) from REO	2,734	(1,440)	8,484	(5,971)
Change in fair value of net trust assets, including trust REO (losses) gains	\$ (1,745)	\$ 1,071	\$ 6,578	\$ 2,609

The change in fair value related to our net trust assets (residual interests in securitizations) was a loss of \$1.7 million for the three months ended September 30, 2017. The change in fair value of net trust assets, excluding REO was due to \$4.5 million in losses from changes in fair value of securitized mortgage borrowings and securitized mortgage collateral primarily associated with an increase in LIBOR, partially offset by updated assumptions on certain later vintage trusts with improved performance. Additionally, the NRV of REO increased \$2.7 million during the period attributed to lower expected loss severities on properties held in the long-term mortgage portfolio during the period.

The change in fair value related to our net trust assets (residual interests in securitizations) was a gain of \$6.6 million for the nine months ended September 30, 2017. The change in fair value of net trust assets, excluding REO was due to \$1.9 million in losses from changes in fair value of securitized mortgage borrowings and securitized mortgage collateral primarily associated with an increase in LIBOR, partially offset by updated assumptions on certain later vintage trusts with improved performance. Additionally, the NRV of REO increased \$8.5 million during the period as a result of lower expected loss severities on properties held in the long-term mortgage portfolio.

Income Taxes

We recorded income tax expense of \$2.1 million and \$3.6 million for the three and nine months ended September 30, 2017, primarily the result of the recognition of a deferred tax liability created by the amortization of an indefinite-life intangible asset (goodwill) and amortization of the deferred charge. The deferred tax liability for indefinite-life intangibles cannot be included in the calculation of valuation allowance as these liabilities cannot be considered when determining the realizability of the net deferred tax assets.

For the three and nine months ended September 30, 2016, we recorded income tax benefit of \$130 thousand and an expense of \$728 thousand, respectively, primarily the result of a return to provision adjustment for the 2015 tax return booked in the third quarter, amortization of the deferred charge, federal alternative minimum tax (AMT), and state income taxes from states where we do not have net operating loss carryforwards or state minimum taxes, including AMT. The deferred charge represents the deferral of income tax expense on inter-company profits that resulted from the sale of mortgages from taxable subsidiaries to IMH prior to 2008. The deferred charge amortization and/or impairment, which does not result in any tax liability to be paid is calculated based on the change in fair value of the underlying securitized mortgage collateral during the period. The deferred charge is included in other assets in the accompanying consolidated balance sheets and is amortized as a component of income tax expense in the accompanying consolidated statements of operations.

[Table of Contents](#)

As of December 31, 2016, we had estimated federal net operating loss (NOL) carryforwards of approximately \$581.8 million. Federal net operating loss carryforwards begin to expire in 2027. As of September 30, 2017, the estimated Federal NOL carryforward expiration schedule is as follows (in millions):

<u>Tax Year Established</u>	<u>Amount</u>	<u>Expiration Date</u>
12/31/2007	\$ 228.8	12/31/2027
12/31/2008	3.6	12/31/2028
12/31/2009	101.6	12/31/2029
12/31/2010	89.7	12/31/2030
12/31/2011	44.1	12/31/2031
12/31/2012	—	12/31/2032
12/31/2013	28.5	12/31/2033
12/31/2014	—	12/31/2034
12/31/2015	30.5	12/31/2035
12/31/2016	55.0	12/31/2036
Total Federal NOLs	\$ 581.8	

As of December 31, 2016, we had estimated California net operating loss (NOL) carryforwards of approximately \$487.0 million, of which \$86.9 million expire in 2017. We may not be able to realize the maximum benefit due to the nature and tax entity that holds the NOL

Results of Operations by Business Segment

We have three primary operating segments: Mortgage Lending, Real Estate Services and Long-Term Mortgage Portfolio. Unallocated corporate and other administrative costs, including the cost associated with being a public company, are presented in Corporate. Segment operating results are as follows:

Mortgage Lending

	<u>For the Three Months Ended September 30,</u>			
	<u>2017</u>	<u>2016</u>	<u>Increase (Decrease)</u>	<u>% Change</u>
Gain on sale of loans, net	\$ 42,476	\$ 113,158	\$ (70,682)	(62)%
Servicing fees, net	8,492	3,789	4,703	124
Loss on mortgage servicing rights, net	(10,513)	(15,857)	5,344	34
Other	—	18	(18)	(100)
Total revenues	40,455	101,108	(60,653)	(60)
Other income	1,106	1,092	14	1
Personnel expense	(21,268)	(37,996)	16,728	44
Business promotion	(10,376)	(10,310)	(66)	(1)
General, administrative and other	(5,018)	(5,578)	560	10
Accretion of contingent consideration	(396)	(1,591)	1,195	75
Change in fair value of contingent consideration	4,798	(23,215)	28,013	121
Earnings before income taxes	\$ 9,301	\$ 23,510	\$ (14,209)	(60)%

For the three months ended September 30, 2017, gain on sale of loans, net were \$42.5 million compared to \$113.2 million in the comparable 2016 period. The \$70.7 million decrease is primarily due to a \$52.8 million decrease in premiums from the sale of mortgage loans, a \$23.0 million decrease in premiums from servicing retained loan sales, a \$6.6 million decrease in mark-to-market gains on LHFS, a \$3.5 million decrease in realized and unrealized net gains on

[Table of Contents](#)

derivative financial instruments and a \$1.8 million increase in provision for repurchases, partially offset by a \$17.2 million decrease in direct loan origination expenses.

The overall decrease in gain on sale of loans, net was primarily due to a 51% decrease in volume as well as a decrease in gain on sale margins. For the three months ended September 30, 2017, we originated and sold \$2.1 billion and \$2.1 billion of loans, respectively, as compared to \$4.2 billion and \$4.1 billion of loans originated and sold, respectively, during the same period in 2016. Margins decreased to approximately 204 bps for the three months ended September 30, 2017 as compared to 268 bps for the same period in 2016 due to margin compression across all three channels as a result of the increase in interest rates as compared to the third quarter of 2016 as well as an increase in competition for volume.

For the three months ended September 30, 2017, servicing fees, net was \$8.5 million compared to \$3.8 million in the comparable 2016 period. The increase in servicing fees, net was the result of the servicing portfolio increasing 81% to an average balance of \$15.4 billion for the three months ended September 30, 2017 as compared to an average balance of \$8.5 billion for the three months ended September 30, 2016. The increase in the average balance of the servicing portfolio is a result of our efforts during the past year to retain servicing with fewer bulk sales of MSR. We had \$1.9 billion in servicing retained loan sales during the three months ended September 30, 2017 with no bulk sales of MSR.

For the three months ended September 30, 2017, loss on MSR, net was \$10.5 million compared to \$15.9 million in the comparable 2016 period. For the three months ended September 30, 2017, we recorded an \$11.2 million loss from a change in fair value of MSR primarily the result of mark-to-market changes related to amortization as well as an increase in prepayment speeds. During the quarter, we had an \$8 thousand loss on sale of mortgage servicing rights related to refunds of premiums to investors for loan payoffs associated with sales of servicing rights in previous periods. Partially offsetting the loss was \$672 thousand in realized and unrealized gains from hedging instruments related to MSR.

For the three months ended September 30, 2017, other income was flat at \$1.1 million compared to the comparable 2016 period. The \$14 thousand increase in other income was due to a \$178 thousand increase in net interest spread between loans held-for-sale, finance receivables and their related warehouse borrowing expense as well as a \$28 thousand increase in interest income on invested cash balances partially offset by a \$192 thousand increase in interest expense related to the MSR financing facility entered into in February 2017.

Personnel expense was \$21.3 million for the three months ended September 30, 2017, compared to \$38.0 million for the comparable period of 2016. The decrease is primarily related to a reduction in commission expense due to a decrease in loan originations as well as staff reductions made in the first quarter of 2017. As a result of the staff reductions in the first quarter of 2017, average headcount of the mortgage lending operations decreased 27% for the third quarter of 2017 as compared to the same period in 2016.

Business promotion was flat at \$10.4 million for the three months ended September 30, 2017 and 2016. Our centralized call center purchases leads and promotes its business through radio and television advertisements. During the third quarter of 2017, business promotion was relatively flat as compared to 2016 with continued efforts to increase NonQM and purchase money production with the reduction in refinance activity as a result of the increase in interest rates as compared to the third quarter of 2016.

General, administrative and other expenses decreased to \$5.0 million for the three months ended September 30, 2017, compared to \$5.6 million for the same period in 2016. The decrease was primarily related to a \$561 thousand decrease in other general and administrative expenses and a \$156 thousand decrease in data processing expense, partially offset by a \$157 thousand increase in occupancy expense.

As part of the acquisition of CCM, we record accretion of the contingent consideration liability from the close of the transaction in March 2015 through the end of the earn-out period in December 2017, which increases the contingent consideration liability. The estimated contingent consideration liability is based on discounted cash flows which represent the time value of money of the liability during the earn-out period. In the third quarter of 2017, accretion increased the contingent consideration liability by \$396 thousand as compared to \$1.6 million during the third quarter of 2016. The decrease in accretion is due to the reduction of forecasted pre-tax earnings of CCM as a result of

[Table of Contents](#)

updated assumptions as well as a reduction in the estimated earn-out percentage as compared to 2016. The accretion will continue to be a charge against earnings in future quarters until the end of the earn-out period in December 2017.

We recorded a \$4.8 million change in fair value associated with a reduction in the contingent consideration liability for the third quarter of 2017 related to updated assumptions including current market conditions. The change in fair value of contingent consideration was primarily related to expected margin compression as well as a reduction in origination volume over the remaining earn-out period which ends in December 2017. The fair value of contingent consideration may change from quarter to quarter based upon actual experience and updated assumptions used to forecast pre-tax earnings for CCM. The decrease in the contingent consideration liability resulted in an increase in earnings of \$4.8 million in the third quarter of 2017.

	For the Nine Months Ended September 30,			
	2017	2016	Increase (Decrease)	% Change
Gain on sale of loans, net	\$ 116,602	\$ 245,849	\$ (129,247)	(53)%
Servicing fees, net	23,575	8,680	14,895	172
Loss on mortgage servicing rights, net	(18,159)	(41,249)	23,090	56
Other	19	70	(51)	(73)
Total revenues	122,037	213,350	(91,313)	(43)
Other income	2,096	2,148	(52)	(2)
Personnel expense	(64,226)	(92,334)	28,108	30
Business promotion	(30,668)	(30,721)	53	0
General, administrative and other	(15,085)	(15,214)	129	1
Accretion of contingent consideration	(1,948)	(5,244)	3,296	63
Change in fair value of contingent consideration	11,052	(34,569)	45,621	132
Earnings before income taxes	\$ 23,258	\$ 37,416	\$ (14,158)	(38)

For the nine months ended September 30, 2017, gain on sale of loans, net were \$116.6 million compared to \$245.8 million in the comparable 2016 period. The \$129.2 million decrease is primarily due to a \$108.3 million decrease in premiums from the sale of mortgage loans, a \$49.1 million decrease in premiums from servicing retained loan sales and an \$11.3 million decrease in mark-to-market gains on LHFS, partially offset by a \$39.6 million decrease in direct loan origination expenses, \$149 thousand decrease in realized and unrealized net losses on derivative financial instruments and a \$586 thousand decrease in provision for repurchases.

The overall decrease in gain on sale of loans, net was primarily due to a 44% decrease in volumes as well as a decrease in gain on sale margins. For the nine months ended September 30, 2017 we originated and sold \$5.5 billion and \$5.3 billion of loans, respectively, as compared to \$9.8 billion and \$9.3 billion of loans originated and sold, respectively, during the same period in 2016. Margins decreased to approximately 214 bps for the nine months ended September 30, 2017 as compared to 251 bps for the same period in 2016 due to margin compression across all three channels as a result of the increase in interest rates as compared to the first nine months of 2016 as well as an increase in competition for volume.

For the nine months ended September 30, 2017, servicing fees, net was \$23.6 million compared to \$8.7 million in the comparable 2016 period. The increase in servicing fees, net was the result of the servicing portfolio increasing 122% to an average balance of \$14.1 billion for the nine months ended September 30, 2017 as compared to an average balance of \$6.4 billion for the nine months ended September 30, 2016. The increase in the average balance of the servicing portfolio is a result of our efforts during the past year to retain servicing with fewer bulk sales of MSRs. We had \$4.7 billion in servicing retained loan sales during the nine months ended September 30, 2017. Partially offsetting the increase was a bulk sale of NonQM MSRs totaling approximately \$155.9 million in UPB.

[Table of Contents](#)

For the nine months ended September 30, 2017, loss on MSRs, net was \$18.2 million compared to \$41.2 million in the comparable 2016 period. For the nine months ended September 30, 2017, we recorded a \$20.0 million loss from a change in fair value of MSRs primarily the result of mark-to-market changes related to amortization as well as an increase in prepayment speeds. During the nine months ended September 30, 2017, we had a \$90 thousand loss on sale of mortgage servicing rights related to refunds of premiums to investors for loan payoffs partially offset by recoveries of previously written off holdbacks associated with sales of servicing rights in previous periods. Partially offsetting the loss was a \$2.0 million increase in realized and unrealized gains from hedging instruments related to MSRs.

For the nine months ended September 30, 2017, other income was flat at \$2.1 million compared to the comparable 2016 period. The \$52 thousand decrease in other income was due to a \$674 thousand increase in interest expense related to the MSR financing facility entered into in February 2017, partially offset by a \$596 thousand increase in net interest spread between loans held-for-sale, finance receivables and their related warehouse borrowing expense as well as a \$28 thousand increase in interest income on invested cash balances.

Personnel expense was \$64.2 million for the nine months ended September 30, 2017, compared to \$92.3 million for the comparable period of 2016. The decrease is primarily related to a reduction in commission expense due to a decrease in loan originations as well as staff reductions made in the first quarter of 2017. With the decline in origination volumes in the first quarter of 2017 we made staff reductions, of which the full impact of the reductions were not reflected until the second quarter. As a result, average headcount decreased 16% for the nine months ended September 30, 2017 as compared to the same period in 2016.

Business promotion was flat at \$30.7 million for the nine months ended September 30, 2017 and the comparable period of 2016. Our centralized call center purchases leads and promotes its business through radio and television advertisements. During the first nine months of 2017, business promotion was flat due to efforts to increase NonQM and purchase money production with the reduction in refinance activity as a result of the increase in interest rates as compared to the first nine months of 2016.

General, administrative and other expenses decreased to \$15.1 million for the nine months ended September 30, 2017, compared to \$15.2 million for the same period in 2016. The decrease was primarily related to a \$693 thousand decrease in other general and administrative expenses and an \$81 thousand decrease in legal and professional fees, partially offset by a \$645 thousand increase in occupancy expense.

As part of the acquisition of CCM, we record accretion of the contingent consideration liability from the close of the transaction in March 2015 through the end of the earn-out period in December 2017, which increases the contingent consideration liability. The estimated contingent consideration liability is based on discounted cash flows which represent the time value of money of the liability during the earn-out period. In the first nine months of 2017, accretion increased the contingent consideration liability by \$1.9 million as compared to \$5.2 million during the first nine months of 2016. The decrease in accretion is due to the reduction of forecasted pre-tax earnings of CCM as a result of updated assumptions as well as a reduction in the estimated earn-out percentage as compared to 2016. The accretion will continue to be a charge against earnings in future quarters until the end of the earn-out period in December 2017.

We recorded an \$11.1 million change in fair value associated with a reduction in the contingent consideration liability for the nine months ended September 30, 2017 related to updated assumptions including current market conditions. The change in fair value of contingent consideration was primarily related to expected margin compression as well as a reduction in origination volume over the remaining earn-out period which ends in December 2017. The fair value of contingent consideration may change from quarter to quarter based upon actual experience and updated assumptions used to forecast pre-tax earnings for CCM. The decrease in the contingent consideration liability resulted in an increase in earnings of \$11.1 million for the nine months ended September 30, 2017.

Real Estate Services

	For the Three Months Ended September 30,			
	2017	2016	Increase (Decrease)	% Change
Real estate services fees, net	\$ 1,355	\$ 2,678	\$ (1,323)	(49)%
Personnel expense	(638)	(1,863)	1,225	66
General, administrative and other	(159)	(142)	(17)	(12)
Earnings before income taxes	<u>\$ 558</u>	<u>\$ 673</u>	<u>\$ (115)</u>	(17)%

For the three months ended September 30, 2017, real estate services fees, net were \$1.4 million compared to \$2.7 million in the comparable 2016 period. The \$1.3 million decrease in real estate services fees, net was the result of a \$1.0 million decrease in loss mitigation fees, a \$302 thousand decrease in real estate and recovery fees and a \$22 thousand decrease in real estate services. The \$1.3 million decrease was primarily the result of a decrease in transactions related to the decline in the number of loans and the UPB of the long-term mortgage portfolio as compared to 2016.

For the three months ended September 30, 2017, the \$1.2 million reduction in personnel expense was due to a reduction in personnel and personnel related costs as a result of a decrease in transactions related to the decline in the number of loans and the UPB of the long-term mortgage portfolio as compared to 2016.

	For the Nine Months Ended September 30,			
	2017	2016	Increase (Decrease)	% Change
Real estate services fees, net	\$ 4,492	\$ 6,773	\$ (2,281)	(34)%
Personnel expense	(2,046)	(4,721)	2,675	57
General, administrative and other	(488)	(507)	19	4
Earnings before income taxes	<u>\$ 1,958</u>	<u>\$ 1,545</u>	<u>\$ 413</u>	27 %

For the nine months ended September 30, 2017, real estate services fees, net were \$4.5 million compared to \$6.8 million in the comparable 2016 period. The \$2.3 million decrease in real estate services fees, net was the result of a \$1.2 million decrease in real estate and recovery fees and a \$1.1 million decrease in loss mitigation fees partially offset by a \$75 thousand increase in real estate services. The \$2.3 million decrease was primarily the result of a decrease in transactions related to the decline in the number of loans and the UPB of the long-term mortgage portfolio as compared to 2016.

For the nine months ended September 30, 2017, the \$2.7 million reduction in personnel expense was due to a reduction in personnel and personnel related costs as a result of a decrease in transactions related to the decline in the number of loans and the UPB of the long-term mortgage portfolio as compared to 2016.

Long-Term Mortgage Portfolio

	For the Three Months Ended September 30,			
	2017	2016	Increase (Decrease)	% Change
Other revenue	\$ 81	\$ 71	\$ 10	14 %
Personnel expense	(3)	(3)	—	0 %
General, administrative and other	(64)	(99)	35	35
Total expenses	(67)	(102)	35	34
Net interest income	919	1,495	(576)	(39)
Change in fair value of long-term debt	104	(8,641)	8,745	101
Change in fair value of net trust assets, including trust REO gains (losses)	(1,745)	1,071	(2,816)	(263)
Total other income (expense)	(722)	(6,075)	5,353	88
Loss before income taxes	<u>\$ (708)</u>	<u>\$ (6,106)</u>	<u>\$ 5,398</u>	<u>88 %</u>

For the three months ended September 30, 2017, net interest income totaled \$919 thousand as compared to \$1.5 million for the comparable 2016 period. Net interest income decreased \$576 thousand for the three months ended September 30, 2017 primarily attributable to a \$596 thousand decrease in net interest spread on the long-term mortgage portfolio as compared to the previous period partially offset by a \$19 thousand decrease in interest expense on the long-term debt. The reduction in interest expense on the long-term debt was due to the aforementioned exchange of trust preferred securities in May 2017, partially offset by an increase in three-month LIBOR as compared to the prior year.

Change in the fair value of long-term debt resulted in income of \$104 thousand for the three months ended September 30, 2017, compared to an \$8.6 million loss for the comparable 2016 period. The decrease in the estimated fair value of long-term debt in the third quarter of 2017 was the result of a slight decrease in the forward LIBOR curve.

The change in fair value related to our net trust assets (residual interests in securitizations) was a loss of \$1.7 million for the three months ended September 30, 2017. The change in fair value of net trust assets, excluding REO was due to \$4.5 million in losses from changes in fair value of securitized mortgage borrowings and securitized mortgage collateral primarily associated with an increase in LIBOR, partially offset by updated assumptions on certain later vintage trusts with improved performance. Additionally, the NRV of REO increased \$2.7 million during the period attributed to lower expected loss severities on properties held in the long-term mortgage portfolio during the period.

	For the Nine Months Ended September 30,			
	2017	2016	Increase (Decrease)	% Change
Other revenue	\$ 209	\$ 183	\$ 26	14 %
Personnel expense	(11)	(14)	3	21 %
General, administrative and other	(242)	(333)	91	27
Total expenses	(253)	(347)	94	27
Net interest income	2,752	4,259	(1,507)	(35)
Loss on extinguishment of debt	(1,265)	—	(1,265)	n/a
Change in fair value of long-term debt	(2,657)	(7,286)	4,629	64
Change in fair value of net trust assets, including trust REO gains (losses)	6,578	2,609	3,969	152
Total other income	5,408	(418)	5,826	1394
Earnings (loss) before income taxes	<u>\$ 5,364</u>	<u>\$ (582)</u>	<u>\$ 5,946</u>	1022 %

For the nine months ended September 30, 2017, net interest income totaled \$2.8 million as compared to \$4.3 million for the comparable 2016 period. Net interest income decreased \$1.5 million for the nine months ended September 30, 2017 primarily attributable to a \$1.2 million decrease in net interest spread on the long-term mortgage portfolio as well as a \$305 thousand increase in interest expense on the long-term debt due to an increase in three-month LIBOR as compared to the prior year.

During the second quarter of 2017, we exchanged 412,264 shares of common stock for trust preferred securities with an aggregate liquidation amount of \$8.5 million. Accrued and unpaid interest on the trust preferred securities was paid in cash in the aggregate amount of approximately \$14 thousand. We recorded a \$1.3 million loss on extinguishment of debt due to stock price appreciation after the agreed upon settlement and before the issuance date of the common stock.

Change in the fair value of long-term debt resulted in an expense of \$2.7 million for the nine months ended September 30, 2017, compared to a \$7.3 million expense for the comparable 2016. The increase in the estimated fair value of long-term debt in 2017 was primarily the result of a decrease in the discount rate attributable to an improvement in our credit profile, financial condition as well as an increase in three-month LIBOR during 2017.

The change in fair value related to our net trust assets (residual interests in securitizations) was a gain of \$6.6 million for the nine months ended September 30, 2017. The change in fair value of net trust assets, excluding REO was due to \$1.9 million in losses from changes in fair value of securitized mortgage borrowings and securitized mortgage collateral primarily associated with updated loss assumptions and recoveries on a certain later vintage multifamily trust with improved performance. Additionally, the NRV of REO increased \$8.5 million during the period as a result of lower expected loss severities on properties held in the long-term mortgage portfolio.

Corporate

The corporate segment includes all compensation applicable to the corporate services groups, public company costs as well as debt expense related to the Convertible Notes, Term Financing and capital leases. This corporate services group supports all operating segments. A portion of the corporate services costs is allocated to the operating segments. The costs associated with being a public company as well as the interest expense related to the Convertible Notes and capital leases are not allocated to our other segments and remain in this segment.

	For the Three Months Ended September 30,			
	2017	2016	Increase (Decrease)	% Change
Interest expense	\$ (480)	\$ (1,283)	803	63 %
Other expenses	(4,250)	(426)	(3,824)	(898)
Net loss before income taxes	<u>\$ (4,730)</u>	<u>\$ (1,709)</u>	<u>\$ (3,021)</u>	<u>(177)%</u>

For the three months ended September 30, 2017, interest expense decreased to \$480 thousand as compared to \$1.3 million for the comparable 2016 period. The \$803 thousand decrease in interest expense was primarily due an \$803 thousand reduction in interest expense related to the payoff of the Term Financing in February 2017.

For the three months ended September 30, 2017, other expenses increased to \$4.3 million as compared to \$426 thousand for the comparable 2016 period. The increase was primarily due to a reduction in allocated corporate expenses in other segments. The corporate expenses also increased due to a \$1.9 million increase in legal and professional fees associated with defending litigation, as discussed in Item 3 of the 2016 10-K and in Item 1 of Part II within this 10-Q, a \$306 thousand increase in personnel costs primarily associated with our increased investment in technology as well as a \$211 thousand increase in healthcare costs.

	For the Nine Months Ended September 30,			
	2017	2016	Increase (Decrease)	% Change
Interest expense	\$ (1,758)	\$ (4,371)	2,613	60 %
Other expenses	(11,863)	(3,551)	(8,312)	(234)
Net loss before income taxes	<u>\$ (13,621)</u>	<u>\$ (7,922)</u>	<u>\$ (5,699)</u>	<u>(72)%</u>

For the nine months ended September 30, 2017, interest expense decreased to \$1.8 million as compared to \$4.4 million for the comparable 2016 period. The \$2.6 million decrease in interest expense was primarily due a \$637 thousand reduction in interest expense related to the conversion of the original \$20.0 million in Convertible Notes to common stock in January 2016 as well as a \$1.9 million decrease in interest expense related to the payoff the Term Financing in February 2017.

For the nine months ended September 30, 2017, other expenses increased to \$11.9 million as compared to \$3.6 million for the comparable 2016 period. The increase was primarily due to an increase in corporate expenses of \$4.0 million during the nine months ended September 30, 2017 as compared to the same period in 2016 and a reduction in allocated corporate expenses in other segments. The increase in corporate expenses is due to a \$1.4 million increase in personnel costs primarily associated with our increased investment in technology, a \$786 thousand increase in healthcare costs as well as a \$2.4 million increase in legal and professional fees associated with defending litigation, as discussed in Item 3 of the 2016 10-K and in Item 1 of Part II within this 10-Q. Partially offsetting the increase was a \$684 thousand decrease in data processing and equipment expense.

ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to a variety of operational and market risks. Refer to the complete discussion of operational and market risks included in Part II, Item 7 of our report on Form 10-K for the year ended December 31, 2016. There has been no material change to the types of market and operational risks faced by us.

Interest Rate Risk

Our interest rate risk arises from the financial instruments and positions we hold. This includes mortgage loans held for sale, MSR and derivative financial instruments. These risks are regularly monitored by executive management that identify and manage the sensitivity of earnings or capital to changing interest rates to achieve our overall financial objectives.

Our principal market exposure is to interest rate risk, specifically changes in long-term Treasury rates and mortgage interest rates due to their impact on mortgage-related assets and commitments. We are also exposed to changes in short-term interest rates, such as LIBOR, on certain variable rate borrowings including our term financing, MSR financing and mortgage warehouse borrowings. We anticipate that such interest rates will remain our primary benchmark for market risk for the foreseeable future.

Our business is subject to variability in results of operations in both the mortgage origination and mortgage servicing activities due to fluctuations in interest rates. In a declining interest rate environment, we would expect our mortgage production activities' results of operations to be positively impacted by higher loan origination volumes and gain on sale margins. Furthermore, with declining rates, we would expect the market value of our MSRs to decline due to higher actual and projected loan prepayments related to our loan servicing portfolio. Conversely, in a rising interest rate environment, we would expect a negative impact on the results of operations of our mortgage production activities but a positive impact on the market values of our MSRs. The interaction between the results of operations of our mortgage activities is a core component of our overall interest rate risk strategy.

We utilize a discounted cash flow analysis to determine the fair value of MSRs and the impact of parallel interest rate shifts on MSRs. The primary assumptions in this model are prepayment speeds, discount rates, costs of servicing and default rates. However, this analysis ignores the impact of interest rate changes on certain material variables, such as the benefit or detriment on the value of future loan originations, non-parallel shifts in the spread relationships between MBS, swaps and U.S. Treasury rates and changes in primary and secondary mortgage market spreads. We use a forward yield curve, which we believe better presents fair value of MSRs because the forward yield curve is the market's expectation of future interest rates based on its expectation of inflation and other economic conditions.

Interest rate lock commitments (IRLCs) represent an agreement to extend credit to a mortgage loan applicant, or an agreement to purchase a loan from a third-party originator, whereby the interest rate on the loan is set prior to funding. Our mortgage loans held for sale, which are held in inventory awaiting sale into the secondary market, and our interest rate lock commitments, are subject to changes in mortgage interest rates from the date of the commitment through the sale of the loan into the secondary market. As such, we are exposed to interest rate risk and related price risk during the period from the date of the lock commitment through the earlier of (i) the lock commitment cancellation or expiration date; or (ii) the date of sale into the secondary mortgage market. Loan commitments generally range between 15 and 60 days; and our holding period of the mortgage loan from funding to sale is typically within 20 days.

We manage the interest rate risk associated with our outstanding IRLCs and mortgage loans held for sale by entering into derivative loan instruments such as forward loan sales commitments or To-Be-Announced mortgage backed securities (TBA Forward Commitments). We expect these derivatives will experience changes in fair value opposite to changes in fair value of the derivative IRLCs and mortgage loans held-for-sale, thereby reducing earnings volatility. We take into account various factors and strategies in determining the portion of the mortgage pipeline (derivative loan commitments) and mortgage loans held for sale we want to economically hedge. Our expectation of how

many of our IRLCs will ultimately close is a key factor in determining the notional amount of derivatives used in hedging the position.

Mortgage loans held-for-sale are financed by our warehouse lines of credit which generally carry variable rates. Mortgage loans held for sale are carried on our balance sheet on average for only 7 to 25 days after closing and prior to being sold. As a result, we believe that any negative impact related to our variable rate warehouse borrowings resulting from a shift in market interest rates would not be material to our consolidated financial statements.

Sensitivity Analysis

We have exposure to economic losses due to interest rate risk arising from changes in the level or volatility of market interest rates. We assess this risk based on changes in interest rates using a sensitivity analysis. The sensitivity analysis measures the potential impact on fair values based on hypothetical changes (increases and decreases) in interest rates.

Our total market risk is influenced by a wide variety of factors including market volatility and the liquidity of the markets. There are certain limitations inherent in the sensitivity analysis presented, including the necessity to conduct the analysis based on a single point in time and the inability to include the complex market reactions that normally would arise from the market shifts modeled.

We used September 30, 2017 market rates on our instruments to perform the sensitivity analysis. The estimates are based on the market risk sensitivity and assume instantaneous, parallel shifts in interest rate yield curves. Management uses sensitivity analysis, such as those summarized below, based on a hypothetical 25 basis point increase or decrease in interest rates, to monitor the risks associated with changes in interest rates. We believe the use of a 50 basis point shift up and down (100 basis point range) is appropriate given the relatively short time period that the mortgage loans pipeline is held on our balance sheet and exposed to interest rate risk (during the processing, underwriting and closing stages of the mortgage loans which can last up to approximately 60 days). We also actively manage our risk management strategy for our mortgage loans pipeline (through the use of economic hedges such as forward loan sale commitments and mandatory delivery commitments) and generally adjust our hedging position daily. In analyzing the interest rate risks associated with our MSRs, management also uses multiple sensitivity analyses (hypothetical 25 and 50 basis point increases and decreases) to review the interest rate risk associated with our MSRs.

At a given point in time, the overall sensitivity of our mortgage loans pipeline is impacted by several factors beyond just the size of the pipeline. The composition of the pipeline, based on the percentage of IRLC's compared to mortgage loans held for sale, the age and status of the IRLC's, the interest rate movement since the IRLC's were entered into, the channels from which the IRLC's originate, and other factors all impact the sensitivity.

These sensitivities are hypothetical and presented for illustrative purposes only. Changes in fair value based on variations in assumptions generally cannot be extrapolated because the relationship of the change in fair value may not be linear.

The following table summarizes the estimated changes in the fair value of our mortgage pipeline, MSRs and related derivatives that are sensitive to interest rates as of September 30, 2017 given hypothetical instantaneous parallel shifts in the yield curve:

	Changes in Fair Value			
	Down 50 bps	Down 25 bps	Up 25 bps	Up 50 bps
Total mortgage pipeline (1)	(609)	(91)	(346)	(1,081)
Mortgage servicing rights (2)	(14,350)	(6,366)	5,061	8,888

- (1) Represents unallocated mortgage loans held for sale, IRLCs and hedging instruments that are considered "at risk" for purposes of illustrating interest rate sensitivity. IRLCs and hedging instruments are considered to be unallocated when we have not committed the underlying mortgage loans for sale.
- (2) Includes hedging instruments used to hedge fair value changes associated with changes in interest rates relating to mortgage servicing rights.

ITEM 4: CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

The Company maintains disclosure controls and procedures (as defined in the Securities Exchange Act of 1934 Rules 13a-15(e) or 15d-15(e)) designed at a reasonable assurance level to ensure that information required to be disclosed in reports filed or submitted under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by the Company in its reports that it files or submits under the Exchange Act is accumulated and communicated to the Company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

As required by Rules 13a-15 and 15d-15 under the Exchange Act, in connection with the filing of this Quarterly Report on Form 10-Q, our management, under the supervision and with the participation of our CEO and CFO, conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rule 13a-15(e). Based on that evaluation, the Company's chief executive officer and chief financial officer concluded that, as September 30, 2017, the Company's disclosure controls and procedures were effective at a reasonable assurance level.

Changes in Internal Control Over Financial Reporting

There has been no change in the Company's internal control over financial reporting during the Company's quarter ended September 30, 2017, that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1: LEGAL PROCEEDINGS

Legal Proceedings

The Company is a defendant in or a party to a number of legal actions or proceedings that arise in the ordinary course of business. In some of these actions and proceedings, claims for monetary damages are asserted against the Company. In view of the inherent difficulty of predicting the outcome of such legal actions and proceedings, the Company generally cannot predict what the eventual outcome of the pending matters will be, what the timing of the ultimate resolution of these matters will be, or what the eventual loss related to each pending matter may be, if any.

In accordance with applicable accounting guidance, the Company establishes an accrued liability for litigation when those matters present loss contingencies that are both probable and estimable. In any case, there may be an exposure to losses in excess of any such amounts whether accrued or not. Any estimated loss is subject to significant judgment and is based upon currently available information, a variety of assumptions, and known and unknown uncertainties. The matters underlying the estimated loss will change from time to time, and actual results may vary significantly from the current estimate. Therefore, an estimate of possible loss represents what the Company believes to be an estimate of possible loss only for certain matters meeting these criteria. It does not represent the Company's maximum loss exposure.

Based on the Company's current understanding of these pending legal actions and proceedings, management does not believe that judgments or settlements arising from pending or threatened legal matters, individually or in the aggregate, will have a material adverse effect on the consolidated financial position, operating results or cash flows of the Company. However, in light of the inherent uncertainties involved in these matters, some of which are beyond the Company's control, and the very large or indeterminate damages sought in some of these matters, an adverse outcome in one or more of these matters could be material to the Company's results of operations or cash flows for any particular reporting period.

The legal matter updates summarized below are ongoing and may have an effect on the Company's business and future financial condition and results of operations:

On April 30, 2012, a purported class action was filed entitled *Marentes v. Impac Mortgage Holdings, Inc.*, alleging that certain loan modification activities of the Company constitute an unfair business practice, false advertising and marketing, and that the fees charged are improper. The complaint seeks unspecified damages, restitution, injunctive relief, attorney's fees and prejudgment interest. Phase one of the trial for this matter has been continued, with the parties scheduled to return to court on November 29, 2017, for a status conference.

The Company is a party to other litigation and claims which are normal in the course of our operations. While the results of such other litigation and claims cannot be predicted with certainty, we believe the final outcome of such matters will not have a material adverse effect on our financial condition or results of operations. The Company believes that it has meritorious defenses to the claims and intends to defend these claims vigorously and as such the Company believes the final outcome of such matters will not have a material adverse effect on its financial condition or results of operations. Nevertheless, litigation is uncertain and the Company may not prevail in the lawsuits and can express no opinion as to their ultimate resolution. An adverse judgment in any of these matters could have a material adverse effect on the Company's financial position and results of operations.

Please refer to IMH's report on Form 10-K for the year ended December 31, 2016 and subsequent quarterly reports for a description of litigation and claims.

ITEM 1A: RISK FACTORS

A decline in the unpaid principal balance of the servicing portfolio and the related estimated fair value of the MSRs could adversely affect our net earnings, financial condition, future servicing fees and our ability to borrow on the Company's MSR financing facilities.

[Table of Contents](#)

The servicing portfolio and the value of the related MSR are sensitive to changes in prevailing interest rates:

- a decrease in interest rates may increase prepayment speeds which may lead to (i) increased amortization expense; (ii) decrease in servicing fees; and (iii) decrease in the value of our MSR;
- an increase in interest rates, together with an increase in monthly payments when an adjustable mortgage loan's interest rate adjusts upward from an initial fixed rate or a low introductory rate, may cause increased delinquency, default and foreclosure. Increased mortgage defaults and foreclosures may adversely affect our business as they increase our expenses and reduce the number of mortgages we service;

Our servicing portfolio is subject to "run off", meaning that mortgage loans serviced by us may be prepaid prior to maturity or repaid through standard amortization of principal. As a result, our ability to maintain the size of our servicing portfolio depends on our ability to retain the right to service the existing residential mortgages or to originate additional mortgages. Significant "run off" could result in decreasing the estimated value of the MSR, which could have an adverse impact on our net earnings.

Our MSR financing facilities generally allow us to borrow up to 55% of the estimated fair value of MSR. A decline in value of the MSR could limit our ability to borrow on these facilities. Limitations on borrowings on these financing facilities imposed by the amount of eligible collateral pledged could affect the borrowing capacity of the facility, which could have an adverse impact on our financial condition.

ITEM 2: UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3: DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4: MINE SAFETY DISCLOSURES

None.

ITEM 5: OTHER INFORMATION

None.

ITEM 6: EXHIBITS

(a)	Exhibits:
10.1	2010 Omnibus Incentive Plan, as amended (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on July 27, 2017).
10.2	Line of Credit Promissory Note with Merchants Bank of Indiana, dated August 17, 2017 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on August 22, 2017).
10.3	Security Agreement executed by Impac Mortgage Corp. in favor of Merchants Bank of Indiana, dated August 17, 2017 (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on August 22, 2017).
31.1	Certification of Chief Executive Officer pursuant to Item 601(b)(31) of Regulation S-K, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Item 601(b)(31) of Regulation S-K, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certifications of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101	The following materials from Impac Mortgage Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended September 30, 2017, formatted in XBRL (Extensible Business Reporting Language): (1) the Condensed Consolidated Balance Sheets, (2) the Condensed Consolidated Statements of Operations, (3) the Condensed Consolidated Statements of Cash Flows, and (4) Notes to Consolidated Financial Statements, tagged as blocks of text.

* This exhibit shall not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934 or otherwise subject to the liabilities of that section, nor shall it be deemed incorporated by reference in any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934, whether made before or after the date hereof and irrespective of any general incorporation language in any filings.

SIGNATURES

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

IMPAC MORTGAGE HOLDINGS, INC.

/s/ TODDR. TAYLOR

Todd R. Taylor
Chief Financial Officer
(authorized officer of registrant and principal financial officer)

November 9, 2017

CERTIFICATION

I, Joseph R. Tomkinson, certify that:

1. I have reviewed this report on Form 10-Q of Impac Mortgage Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a. designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation;
 - d. disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
 - a. all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b. any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ JOSEPH R. TOMKINSON

Joseph R. Tomkinson
Chief Executive Officer
November 9, 2017

CERTIFICATION

I, Todd R. Taylor, certify that:

1. I have reviewed this report on Form 10-Q of Impac Mortgage Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a. designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation;
 - d. disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
 - a. all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b. any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ TODDR. TAYLOR

Todd R. Taylor
Chief Financial Officer
November 9, 2017

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED
PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the report of Impac Mortgage Holdings, Inc. (the "Company") on Form 10-Q for the period ending September 30, 2017 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), each of the undersigned, in the capacities and on the dates indicated below, hereby certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to his knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ JOSEPH R. TOMKINSON

Joseph R. Tomkinson
Chief Executive Officer
November 9, 2017

/s/ TODD R. TAYLOR

Todd R. Taylor
Chief Financial Officer
November 9, 2017
