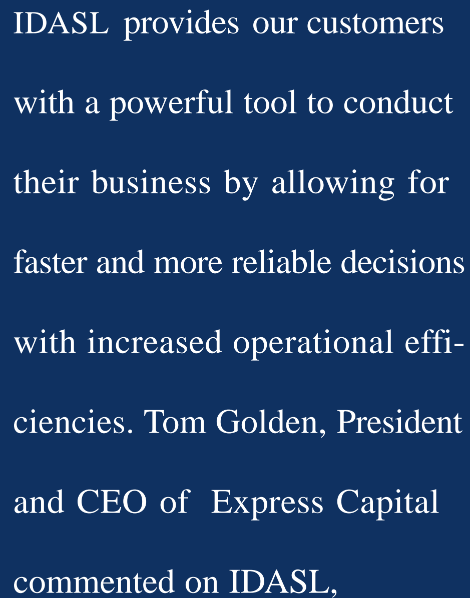
ANNUAL REPORT 1999

ON FORM 10K

This year Impac will revolutionize the mortgage industry and introduce IDASL.com: a web-based mortgage application program that lets brokers get loan approval in minutes.



IDASL provides our customers with a powerful tool to conduct their business by allowing for faster and more reliable decisions with increased operational efficiencies. Tom Golden, President and CEO of Express Capital commented on IDASL,

"It will have a dramatic, positive effect on the way that we execute and deliver the Impac products, both in terms of speed and accuracy. We are adjusting our business to take advantage Impac's new and exciting technology."

We're creating

a revolution in the

mortgage business.

We expect continued

growth in our

operations and

investment portfolio.

Dear Fellow Stockholders:

Following one of the industry's worst years on record, Impac Mortgage Holdings, Inc. ("The Company") eliminated risk of margin calls on its securities portfolio, increased liquidity, restructured its balance sheet and rebounded from a loss in 1998 to earnings of $22.3 million for the year ending December 31, 1999. In addition, the Company accomplished all of its goals as outlined in previous announcements except for the acquisition of the Bank, which the application was re-filed in February 2000. However, in spite of the Company's accomplishments in 1999, the Company's stock continues to hover near the low end of its historical price range.

Therefore, the Company's Board of Directors and the executive team feel it is imperative not only to delineate the 2000 business plan, but also to take the necessary actions to increase long-term shareholder value with a goal to return to historical dividend pay-outs. The 2000 business plan includes a substantial investment in technology, an aggressive expansion of the Company's businesses and a commitment to paying dividends to our loyal stockholders.

Investment in Technology. In 1999, over 70% of our customers used the Internet to conduct business with the Company, such as accessing loan status, pricing, program guidelines, executing rate locks, checking on underwriting dispositions and purchase confirmations. The Company's commitment to technology was evident in 1999 and is forefront in our 2000 business plan.

In 2000, we are aggressively pursuing our business to business technology initiatives to grow our mortgage banking operations with a significant enhancement to our e-commerce business, Impac Direct Access System for Lending ("IDASL"). IDASL is not a lead generator for mortgage brokers, but is an interactive internet-based system that enables our customers to receive automated loan approval decisions, guaranteed pricing and, if necessary, mortgage insurance approval all within less than a minute.

Utilizing our streamlined mortgage loan programs, IDASL is designed to be user friendly, deliver consistent underwriting decisions and reduce the entire process of submitting, underwriting and pricing a mortgage loan from up to several days to a few minutes. Future enhancements to the IDASL system will include the ability to provide fraud detection and electronic property appraisals that will further streamline the entire mortgage application process.

IDASL is now available only to selected customers. By mid year, the Company expects to offer IDASL to mortgage brokers and bankers nationwide.

With the implementation of IDASL, the Company anticipates improved margins, lower cost of originations and increased profitability at all levels of our business operations. Most importantly, IDASL allows the Company to move closer to the borrowers with future minimal capital investment and maintaining centralization, a key factor in our operating strategy.

Business Expansion - The Mortgage Lending Operations. The Company's Mortgage Lending Operations are comprised of The Conduit Operations, Impac Funding Corporation, ("IFC") and the Wholesale/Retail Operations, Impac Lending Group, ("ILG").

The Conduit Operations acquires residential non-conforming loans from originators, including mortgage bankers, credit unions, thrifts and banks, and subsequently securitizes these loans. The implementation of IDASL will enhance the Conduit Operations' profitability by dramatically increasing the efficiencies and speed of underwriting a loan. We expect IDASL to bring competitive advantages to the Conduit Operations, however we anticipate business volumes to remain relatively stable as compared to 1999.

On the other hand, we believe the expansion of our Wholesale/Retail Operations will bring significant future profitability and growth for the Company's mortgage lending operations. The Wholesale/Retail Operations enables residential mortgage brokers and borrowers to access the Company directly to underwrite, fund and close their loans. Direct access to the broker will enable the Company to reduce premiums paid for loans, and thereby considerably improve profitability margins on each loan. Furthermore, IDASL will enable the Company to aggressively expand its operations nationwide while maintaining centralization and a stringent level of quality control.

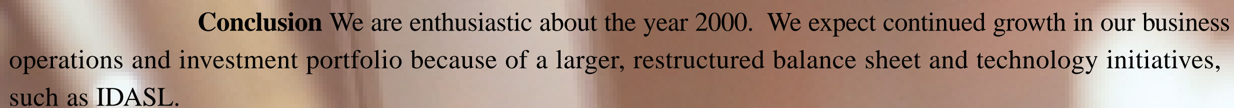
The Warehouse Lending Operations The Warehouse Lending Operations or Impac Warehouse Lending Group, Inc. ("IWLG") provides residential mortgage warehouse lines to smaller mortgage bankers.

The Warehouse Lending Operations requires minimal capital commitment, generates above average market returns and is expected to be a significant contributor to the Company's overall profitability for 2000. During 1999, IWLG increased the number of its customers by 44% and outstanding warehouse lines commitments to $278,000,000. With only a handful of employees, IWLG recorded gross revenues of $33.1 million and net earnings of nearly $9.9 million for the year ending December 31, 1999. During 2000, we expect to continue to add to our customer base, increase our warehouse line commitments and significantly increase average daily outstanding balances.

The Long - Term Investment Operations The Long - Term Investment Operations invests in non-conforming residential mortgage loans and mortgage-backed securities.

During 1999, the Company restructured its balance sheet, increased book value per common share, increased additional liquidity, and improved overall credit quality of its investment portfolio. However, in order to generate consistent long-term earnings and a return to historical dividend pay-outs, the Company must grow its' balance sheet. Therefore, the 2000 business plan includes limiting loan sales to third parties, reducing dividend pay-outs, and retaining the capital to make further investments in the Company's investment portfolio.

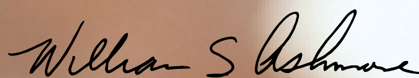
As part of this strategy, the Company has already completed a $460.0 million Collateralized Mortgage Obligation which increased the overall size of the Company's mortgage investment portfolio.



Conclusion We are enthusiastic about the year 2000. We expect continued growth in our business operations and investment portfolio because of a larger, restructured balance sheet and technology initiatives, such as IDASL.

Our mission is to raise market awareness of the Company's operating entities and their underlying value, to rebuild the balance sheet and further increase dividends to our stockholders. We thank you for your continued support and are working diligently to build back stockholder value.

Sincerely,



Joseph R. Tomkinson
Chairman & CEO

William S. Ashmore
President & COO

Financial Highlights

In thousands, except per share data	For the year ended December 31, 1999	1998	1997	1996
Total Assets	$1,675,430	$1,665,504	$1,752,812	$972,355
Net Earnings	$ 22,317	$ (5,933)	$ 28,346 [1]	$ 11,897
Revenues	$ 126,360	$ 150,119	$ 119,859	$ 65,169
Earnings Per Share – Diluted	$ 0.76	$ (0.25)	$ 1.74 [1]	$ 1.34
Dividends Declared Per Share	$ 0.48	$ 1.46	$ 1.68	$ 1.61
Return on Equity	9.29%	(2.48) %	17.38%	16.39%
Return on Assets	1.38%	(0.29) %	2.07%	1.52%
Book Value Per Share [2]	$ 9.76	$ 9.02	$ 10.16	$ 9.62
Market Capitalization Fully Diluted	$ 114,636	$ 139,618	$ 403,000	$148,755
Shares Outstanding Fully Diluted	27,757	30,618	22,546	14,100

[1] Net earnings and earnings per share are stated before a non-recurring charge related to the buyout of the Company's management agreement on December 19, 1997.

[2] Book Value per share calculated assuming liquidation value of the Company's Series B Cumulative Convertible Preferred Stock.

[3] All references to outstanding shares and earnings per share data give retroactive effect to the Company's 3 for 2 stock split effective November 24, 1997.

Key Accomplishments in 1999

Returned to profitability by announcing net earnings of $22.3 million as compared a net loss of $5.9 million in 1998.

Re-established a dividend pay-out by declaring $0.48 per common share for the year.

Increased book value 8% to $9.76 at December 31, 1999 from $9.02 at December 31, 1998.

Restructured Balance Sheet by exchanging 1.4 million shares of common stock for 11% senior subordinated debt, repurchasing 2.0 million shares of common stock, re-securitizing our securities portfolio and retaining for investment $683.3 million of primarily adjustable rate mortgages.

Improved overall credit quality of the mortgage portfolio as a result of lower delinquency rates, higher percentage of prepayment penalties and slower prepayments.

Reduced risk of margin calls by eliminating reliance on short-term borrowings to finance securities portfolio at December 31, 1999.

Increased loan production every quarter in spite of an estimate of a 20% decrease in mortgage originations throughout the Industry.

Introduced Impac Lending Group, our national Wholesale/Retail Lending Operations.

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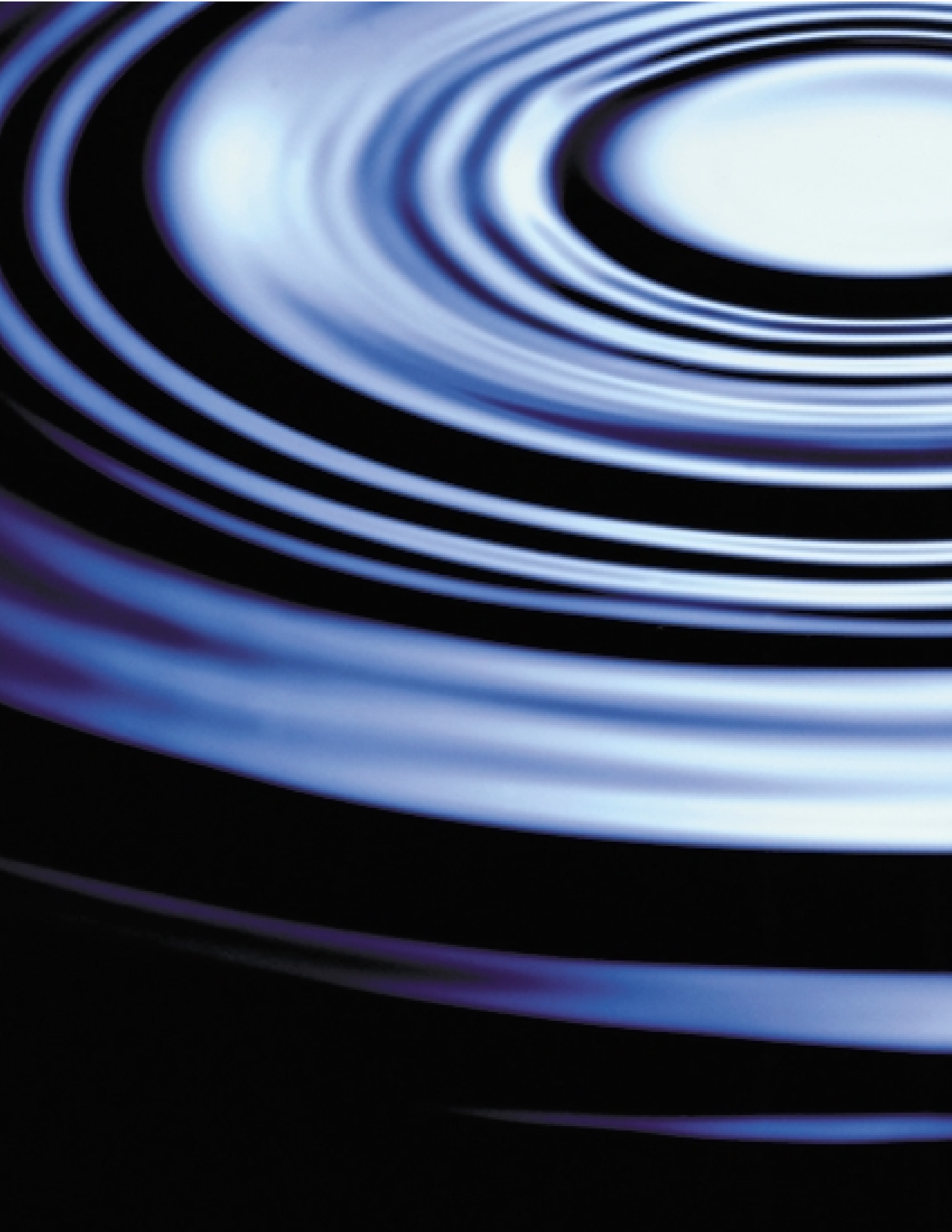

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 1999 or

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from______________ to _____________ .

Commission File Number: 0-19861

IMPAC MORTGAGE HOLDINGS, INC.
(Exact name of registrant as specified in its charter)

Maryland	**33-0675505**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1401 Dove Street, Newport Beach, California 92660
(Address of principal executive offices)

(949) 475-3600
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock $0.01 par value	American Stock Exchange

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

On March 14, 2000, the aggregate market value of the voting stock held by non-affiliates of the registrant was approximately $69.9 million, based on the closing sales price of the Common Stock on the American Stock Exchange. For purposes of the calculation only, in addition to affiliated companies, all directors and executive officers of the registrant have been deemed affiliates. The number of shares of Common Stock outstanding as of March 14, 2000 was 21,400,906.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Definitive Proxy Statement issued in connection with the 2000 Annual Meeting of Stockholders of the Registrant are incorporated by reference into Part III.

IMPAC MORTGAGE HOLDINGS, INC.

1999 FORM 10-K ANNUAL REPORT

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PART I

Certain information contained in this Report constitutes forward-looking statements under the Securities Act and the Exchange Act. These forward-looking statements can be identified by the use of forward-looking terminology including, but not limited to, “may,” “will,” “expect,” “intend,” “should,” “anticipate,” “estimate,” or “believe” or comparable terminology. The Company’s actual results may differ materially from those contained in the forward-looking statements. Factors that might cause such differences include, but are not limited to, those discussed in “Item 1. Business—Risk Factors” as well as those discussed elsewhere in this Report.

ITEM 1. BUSINESS

Impac Mortgage Holdings, Inc. was incorporated in Maryland in August 1995. References to the “Company” refer to Impac Mortgage Holdings, Inc. (“IMH”) and its subsidiaries, IMH Assets Corporation (“IMH Assets”), Impac Warehouse Lending Group, Inc. (“IWLG”), and Impac Funding Corporation, (together with its wholly-owned subsidiary Impac Secured Assets Corporation, (“IFC”)). References to IMH refer to Impac Mortgage Holdings, Inc. as a separate entity from IMH Assets, IWLG and IFC.

General

Impac Mortgage Holdings, Inc. is a mortgage real estate investment trust (“REIT”), which, together with its subsidiaries and related companies, primarily operates three businesses: (1) the Long-Term Investment Operations, (2) the Conduit Operations, and (3) the Warehouse Lending Operations. The Long-Term Investment Operations invests primarily in non-conforming residential mortgage loans and securities backed by such loans. The Conduit Operations purchases and sells and securitizes primarily non-conforming mortgage loans. The Warehouse Lending Operations provides warehouse and repurchase financing to originators of mortgage loans. The Company elects to be taxed as a REIT for federal income tax purposes, which generally allows the Company to pass through income to stockholders without payment of federal income tax at the corporate level.

Long-Term Investment Operations

The Long-Term Investment Operations, conducted by IMH and IMH Assets (a wholly-owned specialty purpose entity through which IMH conducts its CMO borrowings), invests primarily in non-conforming residential mortgage loans and mortgage-backed securities secured by or representing interests in such loans and, to a lesser extent, in second mortgage loans. Non-conforming residential mortgage loans are residential mortgages that generally do not qualify for purchase by government-sponsored agencies such as the Federal National Mortgage Association (“Fannie Mae”) and the Federal Home Loan Mortgage Corporation (“Freddie Mac”). The principal differences between conforming loans and non-conforming loans include applicable loan-to-value ratios, credit and income histories of the mortgagors, documentation required for approval of the mortgagors, type of properties securing the mortgage loans, loan sizes, and the mortgagors' occupancy status with respect to the mortgaged properties. Second mortgage loans are mortgage loans secured by a second lien on the property and made to borrowers owning single-family homes for the purpose of debt consolidation, home improvements, education and a variety of other purposes.

Income is earned primarily from net interest income received by IMH on mortgage loans and mortgage-backed and other collateralized securities acquired and held in its portfolio. Mortgage loans and mortgage-backed and other collateralized securities are financed with capital, borrowings provided from Collateralized Mortgage Obligations (“CMOs”), warehouse facilities, which are referred to as reverse repurchase agreements, and borrowings secured by mortgage-backed securities. IFC supports the investment objectives of the Long-Term Investment Operations by supplying the Long-Term Investment Operations mortgage loans and mortgage-backed securities at prices that are comparable to those available through investment bankers and other third parties.

Mortgage Loans Held in the Portfolio

The Company originates loans through its network of conduit sellers and invests a substantial portion of its portfolio in non-conforming mortgage loans and, to a lesser extent, second mortgage loans. The Company also

purchases such loans from third parties for long-term investment and for resale. Management believes that non-conforming mortgage loans provide an attractive net earnings profile and produce higher yields without commensurately higher credit risks when compared with conforming mortgage loans. A portion of the long-term investment portfolio consists of "A–," "B," "C," and "D" grade mortgage loans, (collectively, "B/C Loans"). The Company believes that a structural change in the mortgage banking industry has occurred which has increased demand for higher yielding non-conforming mortgage loans. This change has been caused by a number of factors, including: (1) investors' demand for higher-yielding assets due to historically low interest rates over the past few years, (2) increased securitization of high-yielding non-conforming mortgage loans by the investment banking industry, (3) quantification and development of standardized credit criteria by credit rating agencies for securities backed by non-conforming mortgage loans, and (4) increased competition in the securitization industry, which has reduced borrower interest rates and fees, thereby making non-conforming mortgage loans more affordable.

Investments in Mortgage-Backed and Other Collateralized Securities

The Company also acquires mortgage-backed securities and other collateralized securities generated through its own securitization efforts and those generated by third parties. In connection with the issuance of mortgage-backed securities by IFC in the form of real estate mortgage investment conduits ("REMICs"), IMH has and may retain senior or subordinated securities as regular interests on a short-term or long-term basis. Such securities or investments may subject the Company to credit, interest rate and/or prepayment risks. In general, subordinated classes of a particular series of securities bear all losses prior to the related senior classes. Losses in excess of expected losses at the time such securities are purchased would adversely affect the Company's yield on such securities and could result in the failure of the Company to recoup its initial investment. The Company may also acquire REMIC or CMO residual interests created through its own securitizations or those of third parties. See "—Conduit Operations—Securitization and Sale Process," and "—Risk Factors—Value of Our Portfolio of Mortgage-Backed Securities May be Adversely Affected."

Financing

The Long-Term Investment Operations are primarily financed through the issuance of CMOs, short-term borrowings under reverse repurchase agreements, borrowings secured by mortgage-backed securities, and proceeds from the sale of capital stock. Refer to "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources" for more information regarding the Company's financing arrangements.

Collateralized Mortgage Obligations. As the Long-Term Investment Operations accumulates mortgage loans in its long-term investment portfolio, the Company may issue CMOs secured by such loans as a means of financing its Long-Term Investment Operations. The decision to issue CMOs is based on the Company's current and future investment needs, market conditions and other factors. For accounting and tax purposes, the mortgage loans financed through the issuance of CMOs are treated as assets of the Company, and the CMOs are treated as debt of the Company, when for accounting purposes the CMO qualifies as a financing arrangement. Each issue of CMOs is fully payable from the principal and interest payments on the underlying mortgage loans collateralizing such debt, any cash or other collateral required to be pledged as a condition to receiving the desired rating on the debt, and any investment income on such collateral. The Long-Term Investment Operations earns the net interest spread between the interest income on the mortgage loans securing the CMOs and the interest and other expenses associated with the CMO financing. The net interest spread may be directly impacted by the levels of prepayment of the underlying mortgage loans and, to the extent each CMO class has variable rates of interest, may be affected by changes in short-term interest rates.

When the Company issues CMOs for financing purposes, it seeks an investment grade rating for such CMOs by a nationally recognized rating agency. To secure such a rating, it is often necessary to pledge collateral in excess of the principal amount of the CMOs to be issued, or to obtain other forms of credit enhancements such as additional mortgage loan insurance. The need for additional collateral or other credit enhancements depends upon factors such as the type of collateral provided, the interest rates paid, the geographic concentration of the mortgaged property securing the collateral, and other criteria established by the rating agencies. The pledge of additional collateral reduces the capacity of the Company to raise additional funds through short-term secured borrowings or additional CMOs, and diminishes the potential expansion of its investment portfolio. As a result, the Company's objective is to pledge additional collateral for

CMOs only in the amount required to obtain an investment grade rating for the CMOs by a nationally recognized rating agency. Total loss exposure to the Company is limited to the equity invested in the CMOs at any point in time.

The Company believes that under prevailing market conditions an issuance of CMOs receiving other than an investment grade rating would require payment of an excessive yield to attract investors. The Company's CMOs typically are structured as one-month London interbank offered rate ("LIBOR") "floaters" and fixed-rate securities with interest payable monthly. Interest rates on adjustable rate CMOs generally range from 0.18% to 8.50% over one-month LIBOR and from 6.65% to 18.25% on fixed rate CMOs depending on the class of the CMOs issued. The CMOs are guaranteed for the holders by a mortgage loan insurer, giving the CMOs the highest rating established by a nationally recognized rating agency.

Reverse Repurchase Agreements. The Company has reverse repurchase agreements at interest rates that are consistent with the Company's financing objectives. A reverse repurchase agreement, although structured as a sale and repurchase obligation, acts as a financing vehicle under which the Company effectively pledges its mortgage loans and mortgage securities as collateral to secure a short-term loan. Generally, the other party to the agreement makes the loan in an amount equal to a percentage of the market value of the pledged collateral. At the maturity of the reverse repurchase agreement, the Company is required to repay the loan and correspondingly receives back its collateral. Under reverse repurchase agreements, the Company retains the instruments of beneficial ownership, including the right to distributions on the collateral and the right to vote on matters as to which certificate holders vote. Upon a payment default under such agreements, the lending party may liquidate the collateral.

The Company's borrowing agreements require the Company to pledge cash, additional mortgage loans or additional securities backed by mortgage loans in the event the market value of existing collateral declines. The Company may be required to sell assets to reduce its borrowings to the extent that cash reserves are insufficient to cover such deficiencies in collateral. To reduce its exposure to the credit risk of reverse repurchase agreement lenders, the Company enters into such agreements with several different parties and follows its own credit exposure procedures. The Company monitors the financial condition of its reverse repurchase agreement lenders on a regular basis, including the percentage of mortgage loans that are the subject of reverse repurchase agreements with a single lender. See "—Risk Factors—Inability to Generate Liquidity May Adversely Affect Our Operations."

Borrowings Secured by Mortgage-Backed Securities. The Company finances a portion of its mortgage-backed securities portfolio with principal only notes. The notes represent senior or subordinated interests in trust funds primarily consisting of a pool of mortgage loans. The notes represent non-recourse obligations of the Company.

Other Mortgage-Backed Securities. As an additional alternative for the financing of its Long-Term Investment Operations, the Company may issue other mortgage-backed securities. The Company may issue mortgage pass-through certificates representing an undivided interest in pools of mortgage loans. The holders of mortgage pass-through certificates receive their pro rata share of the principal payments made on a pool of mortgage loans and interest at a pass-through interest rate that are fixed at the time of offering. The Company may retain up to a 100% undivided interest in a significant number of the pools of mortgage loans underlying such pass-through certificates. The retained interest, if any, may also be subordinated so that, in the event of a loss, payments to certificate holders will be made before the Company receives its payments. Unlike the issuance of CMOs, the issuance of mortgage pass-through certificates will not create an obligation of the Company to security holders in the event of borrower default. However, as in the case of CMOs, the Company may be required to obtain various forms of credit enhancements in order to obtain an investment grade rating for issues of mortgage pass-through certificates by a nationally recognized rating agency.

Conduit Operations

The Conduit Operations, conducted by IFC, purchases primarily non-conforming mortgage loans and, to a lesser extent, second mortgage loans from its network of third party correspondents and other sellers. IFC subsequently securitizes and sells loans to permanent investors, including the Long-Term Investment Operations. All mortgage loans originated or purchased by IFC will be made available for sale to IMH at prices that are comparable to those available through third parties at the date of sale and subsequent transfer to IMH. IMH owns all of the preferred stock of, and 99% of the economic interest in, IFC, while Joseph R. Tomkinson, Chairman and Chief Executive Officer, William S. Ashmore,

President and Chief Operating Officer, and Richard J. Johnson, Executive Vice President and Chief Financial Officer, are the holders of all of the outstanding voting stock of, and 1% of the economic interest in, IFC.

As of February 8, 2000, IFC maintained relationships with 263 correspondents. Correspondents originate and close mortgage loans under IFC's mortgage loan programs on a flow (loan-by-loan) basis or through bulk sale commitments. Correspondents include savings and loan associations, commercial banks, mortgage bankers and mortgage brokers. IFC can compete effectively with other non-conforming mortgage loan conduits through its efficient loan purchasing process, flexible purchase commitment options and competitive pricing and by designing non-conforming mortgage loans to suit the needs of its correspondent loan originators and their borrowers, which are intended to provide sufficient credit quality to its investors. In addition to earnings generated from ongoing securitizations and sales to third-party investors, IFC supports the Long-Term Investment Operations of the Company by supplying IMH with non-conforming mortgage loans and securities backed by such loans.

As a non-conforming mortgage loan conduit, IFC acts as an intermediary between the originators of mortgage loans that do not currently meet the guidelines for purchase by government-sponsored entities that guarantee mortgage-backed securities (i.e. Fannie Mae and Freddie Mac) and permanent investors in mortgage-backed securities secured by or representing an ownership interest in such mortgage loans. IFC also acts as a bulk purchaser of primarily non-conforming mortgage loans. The Company believes that non-conforming mortgage loans provide an attractive net earnings profile, producing higher yields without commensurately higher credit risks when compared to mortgage loans that qualify for purchase by Fannie Mae or Freddie Mac. In addition, based on the Company's experience in the mortgage banking industry and in the mortgage conduit business, the Company believes it provides mortgage loan sellers with an expanded and competitively priced array of non-conforming and, to a lesser extent, B/C Loan products, timely purchasing of loans, mandatory, best efforts and optional rate-lock commitments, and flexible master commitments. See "—Purchase Commitment Process and Pricing."

Marketing and Production

Marketing Strategy. The Company's competitive strategy is to be a low-cost national acquirer of mortgage loans to be held for long-term investment, sold in the secondary market as whole loans or securitized as mortgage-backed securities. A key feature of this approach is the use of a large national network of correspondent originators. This allows the Company to shift the high fixed costs of interfacing with the homeowner to the correspondents. The marketing strategy for the Conduit Operations is designed to accomplish three objectives: (1) attract a geographically diverse group of both large and small correspondent loan originators, (2) establish relationships with such correspondents and facilitate their ability to offer a variety of loan products designed by IFC, and (3) purchase loans and securitize and sell them in the secondary market or to IMH. In order to accomplish these objectives, IFC designs and offers loan products that are attractive to potential non-conforming borrowers and to end-investors in non-conforming mortgage loans and mortgage-backed securities.

IFC has historically emphasized and continues to emphasize flexibility in its mortgage loan product mix as part of its strategy to attract correspondents and establish relationships. IFC also maintains relationships with numerous end-investors so that it may develop products that they may be interested in as market conditions change, which in turn may be offered through the correspondent network. As a consequence, IFC is less dependent on acquiring conforming mortgage loans and has acquired significant volumes of non-conforming loans.

In response to the needs of its non-conforming mortgage loan correspondents, and as part of its strategy to facilitate the sale of its loans through the Conduit Operations, IFC's marketing strategy offers efficient response time in the purchase process, direct and frequent contact with its correspondents through a trained sales force and flexible commitment programs. Finally, due to the price sensitivity of most homebuyers, IFC is competitive in pricing its products in order to attract sufficient numbers of borrowers.

The Progressive Series Loan Program. The underwriting guidelines utilized in the Progressive Series Loan Program ("Progressive Series"), as developed by IFC, are intended to assess the borrower's ability and willingness to repay the mortgage loan obligation and to assess the adequacy of the mortgaged property as collateral for the mortgage loan. Progressive Series is designed to meet the needs of borrowers with excellent credit, as well as those with credit that has been adversely affected. Progressive Series consists of six mortgage loan programs. Each program has different credit

criteria, reserve requirements, qualifying ratios and loan-to-value ratio ("LTV") restrictions. Series I is designed with credit history and income requirements typical of "A" credit borrowers. In the event a borrower does not fit the series I criteria, the borrower's mortgage loan is placed into either series II, III, III+, IV, V or VI, depending on which series' mortgage loan parameters meets the borrower's unique credit profile. Series II, III, III+, IV, V or VI allow for less restrictive standards because of certain compensating or offsetting factors such as a lower LTV, verified liquid assets, job stability, pride of ownership and, in the case of refinance mortgage loans, length of time owning the mortgaged property. The philosophy of Progressive Series is that no single borrower characteristic should automatically determine whether an application for a mortgage loan should be approved or disapproved. Lending decisions are based on a risk analysis assessment after the review of the entire mortgage loan file. Each mortgage loan is individually underwritten with emphasis placed on the overall quality of the mortgage loan. Progressive Series I utilizes an average annual salary to calculate the debt service-to-income ratio. Salaried borrowers are evaluated based on a 12-month salary history while self-employed and commission borrowers are evaluated on a 24-month basis. The debt service-to-income ratio for series I borrowers is required to be within the range of 36% to 50%. Progressive Series II, III, III+, IV, V and VI borrowers are required to have debt service-to-income ratios within the range of 45% to 60% (calculated on the basis of monthly income), depending on the LTV of the mortgage loan.

The Progressive Express Loan Program. In July 1996, IFC developed an additional program to the Progressive Series, called the Progressive Express Loan Program ("Progressive Express"). The concept of Progressive Express is to underwrite loans focusing on the borrower's Fair Isaac Credit Score ("FICO"), the borrower's ability and willingness to repay the mortgage loan obligation, and assessment of the adequacy of the mortgage property as collateral for the loan. The FICO was developed by Fair Isaac Co., Inc. of San Rafael, California. It is an electronic evaluation of past and present credit accounts on the borrower's credit bureau report. This includes all reported accounts as well as public records and inquiries. Progressive Express offers six levels of mortgage loan programs. Progressive Express has a minimum FICO that must be met by the borrower's primary wage earner and does not allow for exceptions to the FICO requirement. The FICO requirement is as follows: Progressive Express I - above 680, Progressive Express II - 680-620, Progressive Express III - 619-601, Progressive Express IV - 600-581, Progressive Express V - 580-551, and Progressive IV - 550-500. Each Progressive Express program has different FICO requirements, credit criteria, reserve requirements, and LTV restrictions. Progressive Express I is designed for credit history and income requirements typical of "A+" credit borrowers. In the event a borrower does not fit the Progressive Express I criteria, the borrower's mortgage loan is placed into either Progressive Express II, III, IV, V, VI, depending on which series' mortgage loan parameters meets the borrowers unique credit profile.

Impac Lending Group ("ILG"). ILG began operations in January 1999 and markets, underwrites, processes and funds mortgage loans for both of the Company's wholesale and retail customers. Through the wholesale division, ILG allows mortgage brokers to work directly with the Company to originate, underwrite and fund their mortgage loans. Many of the Company's wholesale customers cannot conduct business with the Conduit Operations as correspondent sellers because they do not meet the higher net worth requirements. Through the retail division, ILG markets mortgage loans directly to the public. Both the wholesale and retail divisions offer all of the loan programs, including Progressive Series and Progressive Express, that are offered by the Conduit Operations.

Mortgage Loans Acquired. A majority of mortgage loans purchased by the Conduit Operations are non-conforming mortgage loans. Currently, the maximum principal balance for a conforming loan is $252,700. Loans that exceed such maximum principal balance are referred to as "jumbo loans." Non-conforming mortgage loans generally consist of jumbo loans or other loans that are originated in accordance with underwriting or product guidelines that differ from those applied by Fannie Mae and Freddie Mac. Non-conforming loans may involve greater risk as a result of different underwriting and product guidelines. A portion of the mortgage loans purchased through the Conduit Operations are B/C Loans, as described below, which may entail greater credit risks than other non-conforming loans. IFC generally does not acquire mortgage loans with principal balances above $750,000 for "A" quality loans, and $500,000 for B/C Loans. Non-conforming loans purchased by IFC pursuant to its underwriting programs typically differ from those purchased pursuant to the guidelines established by Fannie Mae and Freddie Mac primarily with respect to required documentation, LTV ratios, borrower income or credit history, interest rates, borrower occupancy of the mortgaged property, and/or property types. To the extent that these programs reflect underwriting standards different from those of Fannie Mae and Freddie Mac, the performance of loans made may reflect higher delinquency rates and/or credit losses.

IFC's focus on the acquisition of non-conforming mortgage loans may affect the Company's financial performance. For example, the purchase market of non-conforming loans has typically provided for higher interest rates in order to compensate for the lower liquidity of such loans, thereby potentially enhancing the interest income earned by the Company during the accumulation phase for loans held-for-sale and during the holding period for loans held-for-investment. In addition, due to the lower level of liquidity in the non-conforming loan market, the Company may realize higher returns upon securitization of such loans than would be realized upon securitization of conforming loans. On the other hand, such lower levels of liquidity may from time to time cause the Company to hold such loans or other mortgage-related assets supported by such loans. In addition, by retaining for investment either the loans or other mortgage-related assets supported by such loans, the Company assumes the potential risk of any increased delinquency rates and/or credit losses as well as interest rate risk.

Mortgage loans acquired by IFC are generally secured by first liens and, to a lesser extent, second liens on single (one-to-four) family residential properties with either fixed or adjustable interest rates. Fixed rate mortgage loans ("FRMs") have a constant interest rate over the life of the loan, which is generally 15 or 30 years. The interest rate on adjustable rate mortgage loans ("ARMs") are typically tied to an index, such as six-month LIBOR or the one-year constant maturity Treasury index ("CMT Index") and are adjustable periodically at various intervals. ARMs are typically subject to lifetime interest rate caps and periodic interest rate and/or payment caps. The interest rates on ARMs are typically lower than the average comparable fixed rate loan initially, but may be higher than average comparable fixed rate loans over the life of the loan. Currently, IFC purchases (1) FRMs that have original terms to maturity ranging from 10 to 30 years, (2) ARMs that adjust based on LIBOR or the CMT Index, and (3) 2-year and 3-year FRMs that adjust to six-month ARMs approximately two to three years following origination at an interest rate based upon a defined index plus a spread. Substantially all mortgage loans purchased by IFC fully amortize over their remaining terms. However, IFC may purchase mortgage loans with other interest rate and maturity characteristics.

The credit quality of the loans purchased by IFC varies depending upon the specific program under which such loans are purchased. For example, a principal credit risk inherent in adjustable rate mortgage loans is the potential "payment shock" experienced by the borrower as rates rise, which could result in increased delinquencies and credit losses. In the case of negative amortization mortgage loans, a portion of the interest due accrues to the underlying principal balance of the loan, thereby increasing the LTV ratio of the mortgage loans. As a general rule, mortgage loans with higher LTV ratios are vulnerable to higher delinquency rates given the borrower's lower equity investment in the underlying property. Limited documentation mortgage loans, by contrast, must meet more rigorous criteria for borrower credit quality in order to compensate for the reduced level of lender review with respect to the borrower's earnings history and capacity.

The following table summarizes IFC's mortgage loan acquisitions by type of loan, including net premiums, for the periods shown:

	Year ended December 31, 1999	Year ended December 31, 1998
	(dollars in millions, except for average loan size)	
Non-conforming Loans:		
Volume of loans	$ 1,669.4	$ 2,234.7
Percent of total volume	99.9%	99.4%
Conforming Loans:		
Volume of loans	$ 2.3	$ 13.9
Percent of total volume	0.1%	0.6%
Total Mortgage Loan Acquisitions	$ 1,671.7	$ 2,248.6
Fixed Rate Loans:		
Volume of loans	$ 1,037.0	$ 1,893.2
Percent of total volume	62.0%	84.2%
Adjustable Rate Loans:		

Volume of loans	634.7	355.4
Percent of total volume	38.0%	15.8%
Total Mortgage Loan Acquisitions	$ 1,671.7	$ 2,248.6
Average Loan Size	$ 156,000	$ 128,000

IFC's loan purchase activities are expected to continue to focus on those regions of the country where higher volumes of non-conforming mortgage loans are originated, including California, Florida, New Jersey, New York, Colorado, Nevada, Texas, Georgia, Maryland and Hawaii. The highest concentration of non-conforming mortgage loans purchased by IFC relates to properties located in California and Florida because of generally higher property values and mortgage loan balances. During the years ended December 31, 1999 and 1998, mortgage loans secured by California and Florida properties accounted for approximately 44% and 11%, respectively, and 42% and 8%, respectively, of mortgage loan acquisitions. Of the $1.7 billion in mortgage loans acquired during the year ended December 31, 1999, $880.7 million, or 53%, were acquired from IFC's top ten sellers. During the year ended December 31, 1999, Occidental Mortgage Corporation accounted for $181.7 million, or 11%, of mortgage loans acquired by IFC. No other sellers accounted for more than 10% of the total mortgage loans acquired by IFC during the year ended December 31, 1999. In addition, IFC acquired $5.4 million, or 0.3%, of mortgage loans from Walsh Securities, Inc. ("WSI") and $89.2 million, or 5%, of mortgage loans from ILG, affiliates of the Company. James Walsh, Executive Vice President of WSI, is a Director of the Company. During 1999, ILG operated under the business license of WSI. No sellers other than WSI and ILG are affiliates of the Company.

A portion of the mortgage loans acquired by IFC are comprised of B/C Loans, as defined by the Company. For the year ended December 31, 1999, such loans accounted for 10% of IFC's total loan acquisitions as compared to 23% of IFC's total loan acquisitions during 1998. In general, B/C Loans are residential mortgage loans made to borrowers with lower credit ratings than borrowers of higher quality, or so called "A" grade mortgage loans, and are normally subject to higher rates of loss and delinquency than other non-conforming loans purchased by IFC. As a result, B/C Loans normally bear a higher rate of interest and are typically subject to higher fees (including greater prepayment fees and late payment penalties) than non-conforming loans of "A" quality. In general, greater emphasis is placed upon the value of the mortgaged property and, consequently, the quality of appraisals, and less upon the credit history of the borrower in underwriting B/C Loans than in underwriting "A" grade loans. In addition, B/C Loans are generally subject to lower LTV ratios than "A" grade loans. Under IFC's B/C Loan program, underwriting authority is delegated only to correspondents who meet strict underwriting guidelines established by IFC, see "—Underwriting and Quality Control."

High Loan-to-Value Loans. High loan-to-value loans ("125 Loans") consist of second mortgage loans to qualified borrowers who have limited access to traditional mortgage-related financing generally because of a lack of equity in their homes. The loans are typically closed-end (usually 15 years), fixed rate, fully-amortizing loans secured by a first or second lien on the borrower's primary residence, and are typically used by consumers to pay-off credit card and other unsecured indebtedness. Almost all of these loans are made in excess of the value of the underlying collateral available to secure such loans, up to a maximum of 125% of the property's LTV ratio. During 1997, IFC purchased $576.1 million of 125 Loans from Preferred Credit Corporation, of which the majority of 125 Loans were subsequently sold and securitized. As of December 31, 1999, IFC had outstanding 125 Loans held-for-sale of $193,000.

Purchase Commitment Process and Pricing

Master Commitments. As part of its marketing strategy, IFC has established mortgage loan purchase commitments ("Master Commitments") with sellers that, subject to certain conditions, entitle the seller to sell and obligate IFC to purchase a specified dollar amount of non-conforming mortgage loans over a period generally ranging from six months to one year. The terms of each Master Commitment specify whether a seller may sell loans to IFC on a mandatory, best efforts or optional rate-lock basis. Master Commitments do not generally obligate IFC to purchase loans at a specific price, but rather provide the seller with a future outlet for the sale of its originated loans based on IFC's quoted prices at the time of purchase. Master Commitments specify the types of mortgage loans the seller is entitled to sell to IFC and generally range from $2 million to $50 million in aggregate committed principal amount. The provisions of IFC's Seller/Servicer Guide are incorporated in each of the Conduit Operations' Master Commitments and may be modified by

negotiations between the parties. In addition, there are individualized Master Commitment options available to sellers, which include alternative pricing structures or specialized loan products. In order to obtain a Master Commitment, a seller may be asked to pay a non-refundable up-front or non-delivery fee, or both, to the Company. As of December 31, 1999, IFC had outstanding Master Commitments with 88 sellers to purchase mortgage loans in the aggregate principal amount of $1.9 billion over periods ranging from six months to one year, of which $747.5 million had been purchased or committed to be purchased pursuant to rate-locks.

Sellers who have entered into Master Commitments may sell mortgage loans to the Conduit Operations by executing individual, bulk or other rate-locks (each, a "rate-lock"). Each rate-lock, in conjunction with the related Master Commitment, specifies the terms of the related sale, including the quantity and price of the mortgage loans or the formula by which the price will be determined, the rate-lock type and the delivery requirements. Historically, the up-front fee paid by a seller to IFC to obtain a Master Commitment on a mandatory delivery basis is often refunded pro rata as the seller delivers loans pursuant to rate-locks. Any remaining fee after the Master Commitment expires is retained by the Conduit Operations.

Following the issuance of a specific rate-lock, IFC is subject to the risk of interest rate fluctuations and enters into hedging transactions to diminish such risk. Hedging transactions may include mandatory or optional forward sales of mortgage loans or mortgage-backed securities, interest rate caps, floors and swaps, mandatory forward sales, mandatory or optional sales of futures, and other financial futures transactions. The nature and quantity of hedging transactions are determined by the management of IFC based on various factors, including market conditions and the expected volume of mortgage loan purchases. Deferred hedging gains and losses are presented on IFC's balance sheet in mortgage loans held-for-sale. These deferred amounts are recognized upon the sale or securitization of the related mortgage loans. As of December 31, 1999 and 1998, IFC had $792,000 and $263,000, respectively, of deferred hedging losses included in mortgage loans held-for-sale.

Bulk and Other Rate-Locks. IFC also acquires mortgage loans from sellers that are not purchased pursuant to Master Commitments. These purchases may be made on an individual rate-lock basis. Bulk rate-locks obligate the seller to sell and IFC to purchase a specific group of loans, generally ranging from $1 million to $125 million in aggregate committed principal amount, at set prices on specific dates. Bulk rate-locks enable IFC to acquire substantial quantities of loans on a more immediate basis. The specific pricing, delivery and program requirements of these purchases are determined by negotiation between the parties but are generally in accordance with the provisions of IFC's Seller/Servicer Guide. Due to the active presence of investment banks and other substantial investors in this area, bulk pricing is extremely competitive. Loans are also purchased from individual sellers (typically smaller originators of mortgage loans) who do not wish to sell pursuant to either a Master Commitment or bulk rate-lock. The terms of these individual purchases are based primarily on IFC's Seller/Servicer Guide and standard pricing provisions.

Mandatory, Best-Efforts and Optional Rate-Locks. Mandatory rate-locks require the seller to deliver a specified quantity of loans to IFC over a specified period of time regardless of whether the loans are actually originated by the seller or whether circumstances beyond the seller's control prevent delivery. IFC is required to purchase all loans covered by the rate-lock at prices established at the time of rate-lock. If the seller is unable to deliver the specified loans, it may instead deliver comparable loans approved by IFC within the specified delivery time. Failure to deliver the specified mortgage loans or acceptable substitute loans under a mandatory rate-lock obligates the seller to pay IFC a penalty, and, if IFC's mortgage loan yield requirements have declined, the present value of the difference in yield IFC would have obtained on the mortgage loans that the seller agreed to deliver and the yield available on similar mortgage loans subject to mandatory rate-lock issued at the time of such failure to deliver. In contrast, mortgage loans sold on a best-efforts basis must be delivered to IFC only if they are actually originated by the seller. The best-efforts rate-lock provides sellers with an effective way to sell loans during the origination process without any penalty for failure to deliver. Optional rate-locks give the seller the option to deliver mortgage loans to IFC at a fixed price on a future date and requires the payment of up-front fees to IFC. Any up-front fees paid in connection with optional rate-locks are retained by IFC if the loans are not delivered.

Pricing. IFC sets purchase prices at least once every business day for mortgage loans it acquires for its Conduit Operations based on prevailing market conditions. Different prices are established for the various types of loans, rate-lock periods and types of rate-locks (mandatory or best-efforts). IFC's standard pricing is based on the anticipated price it receives upon sale or securitization of the loans, the anticipated interest spread realized during the accumulation

period, the targeted profit margin and the anticipated issuance, credit enhancement, and ongoing administrative costs associated with such sale or securitization. The credit enhancement cost component of IFC's pricing is established for individual mortgage loans or pools of mortgage loans based upon the characteristics of such loans or loan pools. As the characteristics of the loans or loan pools vary, this cost component is correspondingly adjusted upward or downward to reflect the variation. IFC's adjustments are reviewed periodically by management to reflect changes in the costs of credit enhancement. Adjustments to IFC's standard pricing may also be negotiated on an individual basis under Master Commitments or bulk or individual rate-locks with sellers. See "—Securitization and Sale Process."

Purchase Guidelines, Underwriting Methods, Seller Eligibility and Quality Control

Purchase Guidelines. IFC has developed comprehensive purchase guidelines for the acquisition of mortgage loans by the Conduit Operations. Each loan underwritten assesses the borrower's FICO, ability and willingness to repay the mortgage loan obligation and the adequacy of the mortgaged property as collateral for the mortgage loan. Subject to certain exceptions and the type of loan product, each purchased loan must conform to the loan parameters and eligibility requirements specified in IFC's Seller/Servicer Guide with respect to, among other things, loan amount, type of property, LTV ratio, mortgage insurance, credit history, debt service-to-income ratio, appraisal and loan documentation. IFC also performs a full legal documentation review prior to the purchase of all loans. All mortgage loans originated under IFC's loan programs are underwritten either by employees of IFC or by contracted mortgage insurance companies or delegated conduit sellers.

Underwriting Methods. Under all of IFC's underwriting methods, loan documentation requirements for verifying the borrower's income and assets vary according to LTV ratios and other factors. Generally, as the standards for required documentation are lowered, the borrowers' down payment requirements are increased and the required LTV ratios are decreased. The borrower is also required to have a stronger credit history, larger cash reserves and an appraisal of the property that is validated by an enhanced desk and field review. Lending decisions are based on a risk analysis assessment after the review of the entire mortgage loan file. Each mortgage loan is individually underwritten with emphasis placed on the overall quality of the mortgage loan.

Under the Progressive Series program, IFC underwrites one-to-four family mortgage loans with LTV ratios at origination of up to 95% of the property's appraised value, depending on, among other things, a borrower's credit history, repayment ability and debt service-to-income ratio, as well as the type and use of the mortgaged property. Second lien financing of the mortgaged properties may be provided by lender's other than IFC at origination, however, the combined LTV ratio generally may not exceed 95% of the property's appraised value. Progressive Express has a minimum FICO that must be met by the borrower's primary wage earner and does not allow for exceptions to the FICO requirement. Each Progressive Express program has different FICO requirements, credit criteria, reserve requirements, and LTV ratio restrictions. Under the Progressive Express program, IFC underwrites single family dwellings with LTV ratios at origination of up to 95% of the property's appraised value. In order for the property to be eligible for the Progressive Express, it must be a single family residence (1 unit only), condominium, and/or planned unit development. Under Progressive Express, the borrower must disclose employment and assets on the application, however there is no verification of the information.

IFC uses the program parameters as guidelines only. On a case-by-case basis, IFC may determine that the prospective mortgagor warrants an exception outside the standard program guidelines. An exception may be allowed if the loan application reflects certain compensating factors, including (1) the prospective mortgagor has demonstrated an ability to save and devote a greater portion of income to basic housing needs, (2) the prospective mortgagor may have a potential for increased earnings and advancement because of education or special job training, even if the prospective mortgagor has just entered the job market, (3) the prospective mortgagor has demonstrated an ability to maintain a debt free position, (4) the prospective mortgagor may have short term income that is verifiable but could not be counted as stable income because it does not meet the remaining term requirements, and (5) the prospective mortgagor's net worth is substantial enough to suggest that repayment of the loan is within the prospective mortgagor's ability.

IFC does not publish an approved appraiser list for its correspondent sellers. Conduit sellers may select any appraiser of choice, regardless of the LTV ratio of the related loan, from the seller's approved appraiser list. At the discretion of the underwriter, a full appraisal, an enhanced desk review appraisal, or a field review appraisal may be required.

Seller Eligibility Requirements. Mortgage loans acquired by the Conduit Operations are originated by various sellers, including savings and loan associations, banks, mortgage bankers and other mortgage brokers. Sellers are required to meet certain regulatory, financial, insurance and performance requirements established by IFC before they are eligible to participate in its mortgage loan purchase program, and must submit to periodic reviews by IFC to ensure continued compliance with these requirements. IFC's current criteria for seller participation generally includes a minimum tangible net worth requirement of $300,000, approval as a Fannie Mae or Freddie Mac Seller/Servicer in good standing, a Housing and Urban Development approved mortgagee in good standing or a financial institution that is insured by the Federal Deposit Insurance Corporation ("FDIC") or comparable federal or state agency, and that the seller is examined by a federal or state authority. In addition, sellers are required to have comprehensive loan origination quality control procedures. In connection with its qualification, each seller enters into an agreement that generally provides for recourse by IFC against the seller in the event of a breach of representations or warranties made by the seller with respect to mortgage loans sold to IFC, which includes but is not limited to any fraud or misrepresentation during the mortgage loan origination process or upon early payment default on such loans.

The underwriting program consists of three separate subprograms. IFC's principal delegated underwriting subprogram is a fully delegated program designed for loan sellers that meet higher financial and performance criteria than those applicable to sellers generally. Generally, qualifying sellers have tangible net worth of at least $1.5 million and are granted delegated underwriting authority to a maximum loan amount of $500,000 for all mortgage products under this subprogram. The second subprogram is a delegated program pursuant to which sellers have tangible net worth of $500,000 to $1.5 million and are granted delegated underwriting authority to a maximum loan amount of $300,000. The third program is for sellers with tangible net worth of $300,000 to $500,000 in which sellers are under IFC's non-delegated underwriting program.

IFC has established a delegated underwriting program, which is similar in concept to the delegated underwriting programs established by Fannie Mae and Freddie Mac. Under this program, qualified sellers are required to underwrite loans in compliance with IFC's underwriting guidelines as set forth in IFC's Seller/Servicer Guide and by individual Master Commitment. In order to determine a seller's eligibility to perform under its delegated underwriting program, an internal review is undertaken by IFC's loan committee. In connection with its approval, the seller must represent and warrant to IFC that all mortgage loans sold to IFC will comply with IFC's underwriting guidelines. The current financial, historical loan quality and other criteria for seller participation in this program generally include a minimum net worth requirement and verification of the seller's good standing, including the seller's experience and demonstrated performance, with Fannie Mae and Freddie Mac. IFC periodically reviews the sellers participating in its delegated underwriting program and will retain those sellers that it believes are productive.

Mortgage loans acquired under IFC's non-delegated underwriting program are either fully underwritten by IFC's underwriting staff or involve the use of contract underwriters. IFC has contracted with several national mortgage insurance firms that conduct contract underwriting for mortgage loan acquisitions by IFC. Under these contracts, IFC relies on the credit review and analysis of the contract underwriter, as well as its own pre-purchase eligibility review to ensure that the loan meets program acceptance, its own follow-up quality control procedures, and the representations and warranties of the contract underwriter. Loans that are not acquired under either delegated or contract underwriter methods are fully underwritten by IFC's underwriting staff. In such cases, IFC performs a full credit review and analysis to ensure compliance with its loan eligibility requirements. This review specifically includes, among other things, an analysis of the underlying property and associated appraisal, and an examination of the credit, employment and income history of the borrower. Under all of these methods, loans are purchased only after completion of a legal documentation and eligibility criteria review.

Quality Control. IFC performs a post-closing quality control review on a minimum of 25% of the mortgage loans originated or acquired under the Progressive Series and Progressive Express programs for complete re-verification of employment, income and liquid assets used to qualify for such mortgage loans. Such reviews also include procedures intended to detect evidence of fraudulent documentation and/or imprudent activity during the processing, funding, servicing or selling of the mortgage loans. Verification of occupancy and applicable information is made by regular mail.

Securitization and Sale Process

General. The Conduit Operations primarily utilizes warehouse lines of credit and equity to finance the acquisition of mortgage loans from correspondents. When a sufficient volume of mortgage loans with similar characteristics has been accumulated, generally $100 million to $350 million, IFC will securitize them through the issuance of mortgage-backed securities in the form of REMICs or resell them as bulk whole loan sales. The period between the time IFC commits to purchase mortgage loans and the time it sells or securitizes such mortgage loans generally ranges from 10 to 90 days, depending on certain factors including the length of the purchase commitment period, the loan volume by product type and the securitization process.

Any decision by IFC to issue REMICs or to sell the loans in bulk is influenced by a variety of factors. REMIC transactions are generally accounted for as sales of the mortgage loans and can eliminate or minimize any long-term residual investment in such loans. REMIC securities consist of one or more classes of "regular interests" and a single class of "residual interest." The regular interests are tailored to the needs of investors and may be issued in multiple classes with varying maturities, average lives and interest rates. These regular interests are predominantly senior securities but, in conjunction with providing credit enhancement, may be subordinated to the rights of other regular interests. The residual interest represents the remainder of the cash flows from the mortgage loans (including, in some instances, reinvestment income) over the amounts required to be distributed to the regular interests. In some cases, the regular interests may be structured so that there is no significant residual cash flow, thereby allowing IFC to sell its entire interest in the mortgage loans. As a result, in some cases, all of the capital originally invested in the mortgage loans by the Company is redeployed in the Conduit Operations.

Each series of mortgage-backed securities is typically fully payable from the mortgage assets underlying such series, and the recourse of investors is limited to such assets and any associated credit enhancement features, such as senior/subordinated structures. To the extent the Company holds subordinated securities, the Company generally bears all losses prior to the related senior security holders. Generally, any losses in excess of the credit enhancement obtained are borne by the security holders. Except in the case of a breach of the standard representations and warranties made by the Company when mortgage loans are securitized, such securities are non-recourse to the Company. Typically, the Company has recourse to the sellers of loans for any such breaches, but there are no assurances of the sellers' abilities to honor their respective obligations.

Credit Enhancement. REMICs created by the Conduit Operations are structured so that one or more of the classes of such securities are rated investment grade by at least one nationally recognized rating agency. In contrast to Agency Certificates (pass-through certificates guaranteed by Fannie Mae or Freddie Mac) in which the principal and interest payments are guaranteed by the U.S. government or one of its agencies, securities created by the Conduit Operations do not benefit from any such guarantee. The ratings for the Conduit Operations' REMICs are based upon the perceived credit risk by the applicable rating agency of the underlying mortgage loans, the structure of the securities and the associated level of credit enhancement. Credit enhancement is designed to provide protection to the security holders in the event of borrower defaults and other losses including those associated with fraud or reductions in the principal balances or interest rates on mortgage loans as required by law or a bankruptcy court.

The Conduit Operations can utilize multiple forms of credit enhancement, including special hazard insurance, private mortgage insurance reserve funds, letters of credit, surety bonds, over-collateralization and subordination or any combination of the foregoing. In determining whether to provide credit enhancement through subordination or other credit enhancement methods, the Conduit Operations takes into consideration the costs associated with each method. Ratings of mortgage-backed securities are based primarily upon the characteristics of the pool of underlying mortgage loans and associated credit enhancement. A decline in the credit quality of such pools (including delinquencies and/or credit losses above initial expectations), or of any third-party credit enhancer, or adverse developments in general economic trends affecting real estate values or the mortgage industry, could result in downgrades of such ratings.

In connection with the securitization of B/C Loans, the levels of subordination required as credit enhancement for the more senior classes of securities issued are higher than those with respect to its "A" grade non-conforming loans. Similarly, in connection with the securitization of mortgage loans secured by second liens, the levels of subordination required as credit enhancement for the more senior classes of securities issued are higher than those with respect to its mortgage loans secured by first liens. Thus, to the extent that the Company retains any of the subordinated securities created in connection with such securitizations and losses with respect to such pools of B/C Loans or mortgage loans secured by second liens are higher than expected, the Company's future earnings could be adversely affected.

Master Servicing and Servicing

Master Servicing

General. IFC generally performs the function of master servicer with respect to mortgage loans it sells and securitizes. The master servicer's function includes collecting loan payments from servicers of loans and remitting loan payments, less master servicing fees receivable and other fees, to a trustee or other purchaser for each series of mortgage-backed securities or loans master serviced. In addition, as master servicer, IFC monitors compliance with its servicing guidelines and is required to perform, or to contract with a third party to perform, all obligations not adequately performed by any servicer. A master servicer typically employs servicers to carry out servicing functions. Servicers typically perform servicing functions for the master servicer as independent contractors. In addition, IFC acts as the master servicer for all loans acquired by the Long-Term Investment Operations. With respect to its function as a master servicer for loans owned by IMH, IFC and IMH have entered into agreements having terms substantially similar to those described below for servicing agreements. Master servicing fees range from 0.01% per annum to 0.03% per annum on the declining principal balances of the loans serviced. As of December 31, 1999 and 1998, IFC's master servicing portfolio was $2.9 billion and $3.7 billion, respectively.

IFC offers its sellers of mortgage loans the right to retain servicing. However, in connection with its warehouse line from IWLG, any such servicers of the mortgage loans would have to be approved by IWLG. In the case of servicing retained mortgage loans, the Company will enter into servicing agreements with the sellers of mortgage loans to service the mortgage loans they sell to the Company. Each servicing agreement will require the servicer to service the Company's mortgage loans in a manner generally consistent with Fannie Mae and Freddie Mac guidelines and procedures and with any servicing guidelines promulgated by the Company. Each servicer will collect and remit principal and interest payments, administer mortgage escrow accounts, submit and pursue insurance claims, and initiate and supervise foreclosure proceedings on the mortgage loans serviced. Each servicer will also provide accounting and reporting services required by the Company for such loans. The servicer will be required to follow such collection procedures as are customary in the industry. The servicer may, at its discretion, arrange with a defaulting borrower a schedule for the liquidation of delinquencies, provided primary mortgage insurance coverage is not adversely affected. Each servicing agreement will provide that the servicer may not assign any of its obligations with respect to the mortgage loans serviced for the Company, except with the Company's consent.

The following table summarizes delinquency statistics for IFC's master servicing portfolio based on principal balance for the periods shown (dollars in millions):

	At December 31, 1999		At December 31, 1998	
	Principal Balance of Loans	% of Master Servicing Portfolio	Principal Balance of Loans	% of Master Servicing Portfolio
Loans delinquent for:				
30-59 days	$ 128.4	4.46%	$ 172.7	4.65%
60-89 days	30.8	1.07	46.7	1.26
90 days	21.1	0.73	51.5	1.39
	180.3	6.26	270.9	7.30
Foreclosures pending	47.0	1.64	54.7	1.47
Bankruptcies pending	26.9	0.93	25.9	0.70
Total delinquencies, foreclosures and bankruptcies	$ 254.2	8.83%	$ 351.5	9.47%

Master Servicing Fees. The Company expects from time to time to retain master servicing fees receivable. Master servicing fees receivable have characteristics similar to "interest-only" securities; accordingly, they have many of the same risks inherent in "interest-only" securities, including the risk that they will lose a substantial portion of their value as a result of rapid prepayments occasioned by declining interest rates. Master servicing fees receivable represent the present value of the difference between the interest rate on mortgage loans purchased by the Conduit Operations and the interest rate received by investors who purchase the securities backed by such loans, in excess of the normal loan

servicing fees charged by either (1) the Conduit Operations on loans acquired "servicing released" or (2) correspondents who sold loans to the Conduit Operations with "servicing retained" (the "Excess Servicing Fees"). At December 31, 1999 and 1998, the Company had no master servicing fees receivable.

To the extent that servicing fees on a mortgage loan exceed an adequate compensation (typically ranging from 0.25% to 0.50% per annum of the mortgage loan principal amount), the Conduit Operations will generate master servicing fees receivable as an asset that represents an estimated present value of those excess fees assuming a certain prepayment rate on the mortgage loan. In determining present value of future cash flows, the Conduit Operations will use a market discount rate. Prepayment assumptions will be based on recent evaluations of the actual prepayments of the Conduit Operations' servicing portfolio or on market prepayment rates on new portfolios on which the Conduit Operations has no experience and the interest rate environment at the time the master servicing fees receivable are created. Management of the Company believes that, depending upon the level of interest rates from time to time, investments in current coupon master servicing fees receivable may be prudent, and if interest rates rise, these investments will mitigate declines in income that may occur in the Conduit Operations. IFC intends to hold the master servicing fees receivable for investment. Currently, the secondary market for master servicing fees receivable is limited. Accordingly, if IFC had to sell these receivables, the value received may or may not be at or above the values at which IFC carried them on its balance sheet.

Servicing

General. IFC subcontracts all of its servicing obligations under such loans to independent third parties pursuant to sub-servicing agreements. IFC believes that the selection of third-party sub-servicers is more effective than establishing a servicing department within the Company. However, part of IFC's responsibility is to continually monitor the performance of the sub-servicers through monthly performance reviews and regular site visits. Depending on these sub-servicer reviews, the Company may in the future rely on its internal collection group to take an ever more active role to assist the sub-servicer in the servicing of these loans. Servicing includes collecting and remitting loan payments, making required advances, accounting for principal and interest, holding escrow or impound funds for payment of taxes and insurance, if applicable, making required inspections of the mortgaged property, contacting delinquent borrowers, and supervising foreclosures and property dispositions in the event of unremedied defaults in accordance with the Company's guidelines. Servicing fees range from 0.25% per annum for FRMs to 0.50% per annum for B/C Loans and ARMs on the declining principal balances of loans serviced.

IFC generally acquires substantially all of its loans on a "servicing released" basis, particularly in the case of the acquisition of B/C Loans due to its belief that control over the servicing and collection functions with respect to B/C Loans is important to the realization of a satisfactory return, and thereby acquires the servicing rights. To the extent IFC finances the acquisition of such loans with its warehouse line with IWLG, IFC pledges such loans and the related servicing rights to IWLG as collateral. As a result, IWLG has an absolute right to control the servicing of such loans (including the right to collect payments on the underlying mortgage loans) and to foreclose upon the underlying real property in the case of default. Typically, IWLG delegates its right to service the mortgage loans securing the warehouse line to IFC.

The following table summarizes certain information regarding IFC's servicing portfolio of mortgage loans for the periods shown (dollars in millions, except average loan size):

	Year ended December 31, 1999	Year ended December 31, 1998
Beginning servicing portfolio	$ 3,714.0	$ 3,028.6
Add: Loan acquisitions	1,647.7	2,198.3
Less: Servicing transferred (1)	(2,270.8)	—
Principal paydowns (2)	(697.5)	(1,512.9)
Ending servicing portfolio	$ 2,393.4	$ 3,714.0
Number of loans serviced	22,096	33,414
Average loan size	$ 108,000	$ 111,000
Weighted average interest rate	9.43%	9.47%

(1) Includes loan sales on a servicing released basis of $1.5 billion and the sale of servicing rights on the unpaid principal balance of $784.3 million. When loans are sold from the servicing portfolio on a servicing released basis, the Company generally sub-services such loans from the sales contract date to the transfer date. When servicing rights on loans are sold, the Company generally retains its function as master servicer.
(2) Includes normal principal runoff and principal prepayments.

Mortgage Servicing Rights. When the Conduit Operations purchases loans which include the associated servicing rights, the allocated price paid for the servicing rights is reflected on its financial statements as Mortgage Servicing Rights ("MSRs"). MSRs differ from master servicing fees receivable primarily by the required amount of servicing to be performed, the loss exposure to the owner of the instrument, and the financial liquidity of the instrument. In contrast to MSRs, where the owner of the instrument acts as the servicer, master servicing fees receivable do not require the owner of the instrument to service the underlying mortgage loan. In addition, master servicing fees receivable subject their owners to greater loss exposure from delinquencies or foreclosure on the underlying mortgage loans than MSRs because a master servicer stands behind the servicer (or sub-servicer) and potentially the owner of the mortgage loan in priority of payment. Both MSRs and master servicing fees receivable are purchased and sold in the secondary markets. However, MSRs are generally more liquid and can be sold at less of a discount as compared to master servicing fees receivable. During periods of declining interest rates, prepayments of mortgage loans increase as homeowners look to refinance at lower rates, resulting in a decrease in the value of the Company's MSRs. Mortgage loans with higher interest rates are more likely to result in prepayments. At December 31, 1999 and 1998, IFC had $15.6 million and $14.1 million, respectively, of MSRs.

Warehouse Lending Operations

The Warehouse Lending Operations, conducted by IWLG, provides warehouse and repurchase financing to affiliated companies and to approved mortgage banks, most of which are correspondents of IFC, to finance mortgage loans during the time from the closing of the loans to their sale or other settlement with pre-approved investors. Generally, the non-conforming mortgage loans funded with such warehouse lines of credit are acquired by IFC. IWLG's warehouse lines are non-recourse and IWLG can only look to the sale or liquidation of the mortgage loans as a source of repayment. Any claim of IWLG as a secured lender in a bankruptcy proceeding may be subject to adjustment and delay. Borrowings under the warehouse facilities are presented on the Company's balance sheets as finance receivables. IFC's outstanding warehouse line balances on IWLG's balance sheet are structured to qualify under REIT asset tests and to generate income qualifying under the 75% gross income test. Terms of affiliated warehouse lines are based on Bank of America's prime rate with advance rates between 90% and 98% of the fair value of the mortgage loans outstanding. Outstanding warehouse line balances to non-affiliates on IWLG's balance sheet do not qualify under REIT asset tests and do not generate income qualifying under the 75% gross income test. Terms of non-affiliated warehouse lines, including the commitment amount, are determined based upon the financial strength, historical performance and other qualifications of the borrower. See "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources—Conduit Operations" for a more detailed discussion of IWLG's warehouse line to IFC.

Regulation

The rules and regulations applicable to the Conduit Operations, among other things, prohibit discrimination and establish underwriting guidelines that include provisions for inspections and appraisals, require credit reports on prospective borrowers, and fix maximum loan amounts. Mortgage loan acquisition activities are subject to, among other laws, the Equal Credit Opportunity Act, Federal Truth-in-Lending Act and the Real Estate Settlement Procedures Act and the regulations promulgated that prohibit discrimination and require the disclosure of certain basic information to mortgagors concerning credit terms and settlement costs. IFC is an approved Fannie Mae and Freddie Mac seller/servicer. IFC is subject to the rules and regulations of Fannie Mae and Freddie Mac with respect to acquiring, processing, selling and servicing conforming mortgage loans. In addition, IFC is required annually to submit to Fannie Mae and Freddie Mac audited financial statements, and each regulatory entity has its own financial requirements for sellers/servicers. For any conforming mortgage loan activities, IFC's affairs are also subject to examination by Fannie Mae and Freddie Mac at any time to assure compliance with the applicable regulations, policies and procedures. Additionally, there are various state and local laws and regulations affecting the Conduit Operations. Mortgage

operations also may be subject to applicable state usury statutes. The Company is presently in material compliance with all material rules and regulations to which it is subject.

Competition

In purchasing non-conforming mortgage loans and issuing securities backed by such loans, the Company competes with established mortgage conduit programs, investment banking firms, savings and loan associations, banks, thrift and loan associations, finance companies, mortgage bankers, insurance companies, other lenders and other entities purchasing mortgage assets. The continued consolidation in the mortgage banking industry may also reduce the number of current sellers available to the Conduit Operations, thus reducing the Company's potential customer base, resulting in IFC's purchasing a larger percentage of mortgage loans from a smaller number of sellers. Such changes could negatively impact the Conduit Operations. Mortgage-backed securities issued by the Conduit Operations and the Long-Term Investment Operations face competition from other investment opportunities available to prospective investors. The Company faces competition in its Conduit Operations and Warehouse Lending Operations from other financial institutions, including but not limited to banks and investment banks. Many of the institutions with which the Company competes in its Conduit Operations and Warehouse Lending Operations have significantly greater financial resources than the Company. However, IFC can compete effectively with other non-conforming mortgage loan conduits through its efficient loan purchasing process, flexible purchase commitment options and competitive pricing and by designing non-conforming mortgage loans to suit the needs of its correspondent loan originators and their borrowers, while providing sufficient credit quality to its investors.

Employees

As of December 31, 1999, the Company had 185 employees, 13 of which were employed by IWLG. Employees and operating management of the Long-Term Investment Operations and Conduit Operations are employed by IFC. As of December 31, 1999, IFC had 172 employees. The Company believes that relations with its employees are good. The Company is not a party to any collective bargaining agreement.

Risk Factors

In addition to the other information in this Form 10-K, the following factors should be considered in evaluating the Company and its business.

Inability to Generate Liquidity May Adversely Affect Our Operations

We must access liquidity to continue our operations, grow our asset base and pay dividends. We have traditionally derived our liquidity from three sources:

- financing facilities provided to us by others to acquire mortgage assets;
- whole loan sales and securitizations of acquired mortgage loans; and
- sale of equity securities.

Margin Calls on Financing Facilities May Adversely Affect Our Operations

Prior to the fourth quarter of 1998, we generally had no difficulty in obtaining favorable financing facilities or in selling acquired mortgage loans. However, during the fourth quarter of 1998 the mortgage industry experienced substantial turmoil as a result of a lack of liquidity in the secondary markets. At that time, investors expressed unwillingness to purchase interests in securitizations due in part to:

- higher than expected credit losses on many companies' securitization interests, and
- the widening of returns expected by institutional investors on securitization interests over the prevailing Treasury rate.

As a result, many mortgage loan originators, including our company, were unable to access the securitization market on favorable terms, which resulted in some companies declaring bankruptcy. Originators, like our company, were

required to sell loans on a whole loan basis and liquidate holdings of mortgage-backed securities to repay financing facilities. However, the large influx of loans available for sale on a whole loan basis affected the pricing offered for these loans which in turn reduced the value of the collateral underlying the financing facilities. Therefore, many providers of financing facilities initiated margin calls. Margin calls resulted when our lenders evaluated the market value of the collateral securing our financing facilities and required us to provide them with additional equity or collateral to secure our borrowings.

Our financing facilities are short-term borrowings and due to the turmoil in the mortgage industry during the latter part of 1998 many traditional providers of financing facilities were unwilling to provide facilities on favorable terms, or at all. If we cannot renew or replace maturing borrowings, we may have to sell, on a whole loan basis, the loans securing these facilities which, depending upon market conditions, may result in substantial losses.

Dependence on Securitizations for Liquidity

We rely significantly upon securitizations to generate cash proceeds to repay borrowings and to create credit availability. Any reduction in our ability to complete securitizations may require us to utilize other sources of financing, which may be on less than favorable terms. In addition, gains on sales from our securitizations represent a significant portion of our earnings. Several factors could affect our ability to complete securitizations of our mortgages, including:

- conditions in the securities markets;
- the credit quality of the mortgage loans originated or purchased by our Conduit Operations;
- the volume of our mortgage loan originations and purchases; and
- our ability to obtain credit enhancement.

If we are unable to profitably securitize a significant number of our mortgage loans in a particular financial reporting period, then it could result in lower income or a loss for that period. As a result of turmoil in the securitization market during the latter part of 1998, many mortgage lenders, including our company, were required to sell mortgage loans on a whole loan basis under adverse market conditions in order to generate liquidity. Many of these sales were made at prices lower than our carrying value of the mortgage loans and we experienced losses. We cannot assure you that we will be able to continue to profitably sell our loans on a whole loan basis, or at all.

Gains on sales from our securitizations have historically represented a substantial portion of our earnings. Our ability to complete securitizations is dependent upon general conditions in the securities and secondary markets and the credit quality of the mortgage loans. In addition, delays in closing sales of our loans increases our risk by increasing the warehousing period for the loans, further exposing our company to credit risk.

The market for first loss risk securities (securities that first take a loss when mortgages are not paid by the borrowers) is generally limited. In connections with our securitizations, we will endeavor to sell all securities subjecting us to a first loss risk. If we cannot sell these securities, then we may be required to hold them for an extended period, subjecting us to a first loss risk.

Inability to Access Capital Markets May Adversely Affect Our Liquidity and Operations

Although we believe our current operating cash flows are sufficient to fund our lending activities and the growth of our mortgage assets, to repay our financing facilities and to pay cash dividends, we continue to explore alternatives for increasing our liquidity through additional asset sales and capital raising efforts. However, we cannot assure you that any of these alternatives will be available to us, or if available, that we will be able to negotiate favorable terms. If we cannot raise cash by selling debt and equity securities, we may be forced to sell our assets at unfavorable prices or discontinue various business activities. Our inability to access the capital markets could have a negative impact on our earnings and ability to pay dividends.

REIT provisions of the Internal Revenue Code require us to distribute to our stockholders substantially all of our taxable income. These provisions restrict our ability to retain earnings and renew capital for our business activities. We may decide in future periods not to be treated as a REIT, which would cause us to be taxed at the corporate level and to cease paying regular dividends. Also, to date a large portion of our dividends to stockholders consisted of distributions

by our Conduit Operations subsidiary to our Long-Term Investment Operations entity. However, our Conduit Operations was not, and is not, required under the REIT provisions to make these distributions. Since we are trying to retain earnings for future growth, we may not cause our Conduit Operations subsidiary to make these distributions in the future. This would materially affect the amount of dividends, if any, paid by us to our stockholders.

Our Prior History is Not Reflective of Future Performance

Our historical financial performance is of limited relevance in predicting our future performance. We began our operations in November 1995. Our future operating results will depend largely upon our ability to expand our long-term investment operations, our conduit operations and our warehouse lending operations. We cannot assure you that we will be able to successfully grow or that our operations will be profitable in the future. We cannot assure you that any prior rates of growth can be sustained or that they are indicative of future results. It is unlikely that any of our future dividends will be equal to or more than those dividends we have paid in the past.

The loans we purchased to date and included in our securitizations have been outstanding for a relatively short period of time and our delinquency and loss experience to date may not be indicative of future results. It is unlikely that we will be able to maintain our delinquency and loan loss ratios at their present levels as our portfolio becomes more seasoned.

Our Borrowings and Substantial Leverage May Cause Losses

Risks of Use of Collateralized Mortgage Obligations

To grow our investment portfolio, we borrow a substantial portion of the market value of substantially all of our investments in mortgage loans and mortgage-backed securities. We currently prefer to use collateralized mortgage obligations as financing vehicles to increase our leverage, since mortgage loans held for collateralized mortgage obligation collateral are retained for investment rather than sold in a secondary market transaction. Retaining mortgage loans as collateralized mortgage obligation collateral exposes our operations to greater credit losses than the use of securitization techniques that are treated as sales. In creating a collateralized mortgage obligation, we make a cash equity investment to fund collateral in excess of the amount of the securities issued. If we experience credit losses on the pool of loans subject to the collateralized mortgage obligation greater than we expected, the value of our equity investment decreases and we would have to adjust the value of the investment in our financial statements.

Cost of Borrowings May Exceed Return on Assets

The cost of borrowings under our financing facilities corresponds to a referenced interest rate plus or minus a margin. The margin varies depending on factors such as the nature and liquidity of the underlying collateral and the availability of financing in the market. We will experience net interest losses if the returns on our assets financed with borrowed funds fail to cover the cost of our borrowings.

Default Risks Under Financing Facilities

If we default under our collateralized borrowings, our lenders could force us to liquidate the collateral. If the value of the collateral is less than the amount borrowed, we would be required to pay the difference in cash. If we were to declare bankruptcy, some of our reverse repurchase agreements may obtain special treatment and our creditors would then be allowed to liquidate the collateral without any delay. On the other hand, if a lender with whom we have a reverse repurchase agreement declares bankruptcy, we might experience difficulty repurchasing our collateral, or enforcing our claim for damages, and it is possible that our claim could be repudiated and we could be treated as an unsecured creditor. If this occurs, our claims would be subject to significant delay and we may receive substantially less than our actual damages.

Risk of Lack of Return of Investment on Liquidation

We have pledged a substantial portion of our assets to secure the repayment of collateralized mortgage obligations issued in securitizations, our financing facilities or other borrowings. We will also pledge substantially all of our current

and future mortgage loans to secure borrowings pending their securitization or sale. The cash flows we receive from our investments that have not yet been distributed, pledged or used to acquire mortgage loans or other investments may be the only unpledged assets available to our unsecured creditors and you if our company were liquidated.

Interest Rate Fluctuations May Adversely Affect Our Operating Results

Our operations, each as a mortgage loan originator and warehouse lender, may be adversely affected by rising and falling interest rates. Higher interest rates may discourage potential borrowers from refinancing mortgages, borrowing to purchase homes or seeking second mortgages. This may decrease the amount of mortgages available to be acquired by our conduit operations and decrease the demand for warehouse financing provided by our warehouse lending operations to originators of mortgage loans. If short-term interest rates exceed long-term interest rates, there is a higher risk of increased loan prepayments, as borrowers may seek to refinance their mortgage loans at lower long-term interest rates. Increased loan prepayments could lead to a reduction in the number of loans we service, the fees we receive for loan servicing and our loan servicing income.

We are subject to the risk of rising mortgage interest rates between the time we commit to purchase mortgages at a fixed price and the time we sell or securitize those mortgages. An increase in interest rates will generally result in a decrease in the market value of mortgages that we have committed to purchase at a fixed price, but have not yet sold or securitized.

Risks of Repricing of Assets and Liabilities

Our principal source of revenue is net interest income or net interest spread, which is the difference between the interest we earn on our interest earning assets and the interest we pay on our interest bearing liabilities. The rates we pay on our borrowings are independent of the rates we earn on our assets and may be subject to more frequent periodic rate adjustments. Therefore, we could experience a decrease in net interest income or a net interest loss because the interest rates on our borrowings could increase faster than the interest rates on our assets. If our net interest spread becomes negative, we will be paying more interest on our borrowings than we will be earning on our assets and we will be exposed to a significant risk of loss.

Additionally, the rates paid on our borrowings and the rates received on our assets may be based upon different indices (i.e., LIBOR, U.S. Treasuries, etc.). If the index used to determine the rate on our borrowings increases faster than the index used to determine the rate on our assets, we will experience a declining net interest spread which will have a negative impact on our profitability and may result in losses.

Risks of Adjustable Rate Mortgages

A significant portion of the mortgage assets held by our long-term investment operations are adjustable rate mortgages or bear interest based upon short-term interest rate indices. We generally fund these mortgage assets with borrowings. To the extent that there is a difference between the interest rate index used to determine the interest rate on our adjustable rate mortgage assets and the interest rate index used to determine the borrowing rate for our related financing, our business may be negatively impacted.

Interest Rate Caps

Adjustable rate mortgages typically have interest rate caps which limit interest rates charged to the borrower during any given period. Our borrowings are not subject to similar restrictions. In a period of rapidly increasing interest rates, the interest rates we pay on our borrowings could increase without limitation, while the interest rates we earn on our adjustable rate mortgage assets would be capped. If this occurs, our net earnings could be significantly reduced or we could suffer a net interest loss.

Payment Caps

Some of our adjustable rate mortgages may be subject to payment caps meaning some portion of the interest accruing on the mortgage is deferred and added to the principal outstanding. Our borrowings do not have similar

provisions. This could cause us to receive less cash on our adjustable rate assets than the interest due on our related borrowings. Also, the increased principal amount outstanding as a result of interest deferral may result in a higher rate of defaults on these loans.

Our Quarterly Operating Results May Fluctuate

Our results of operations, and more specifically our earnings, may significantly fluctuate from quarter to quarter based on several factors, including:

- changes in the amount of loans we originate;
- differences between our cost of funds on borrowings and the average interest rates earned on our loans;
- inability or decisions not to complete significant bulk whole loan sales or securitizations in a particular quarter; and
- problems generally affecting the mortgage loan industry.

A delay in closing a particular mortgage loan sale or securitization would also increase our exposure to interest rate fluctuations by lengthening the period during which our variable rate borrowings under our warehouse facilities are outstanding. If we were unable to sell a sufficient number of mortgage loans at a premium during a particular reporting period, our revenues for that period would decline, which could have a material adverse affect on our operations. As a result, our stock price could also fluctuate.

Our Share Prices Have Been and May Continue to be Highly Volatile

Historically, the market price of our common stock has been extremely volatile. During the fourth quarter of 1998 our stock reached a high of $13.50 and a low of $2.75. On December 31, 1999, the closing sale price was $4.13. The market price of our common stock is likely to continue to be highly volatile and could be significantly affected by factors including:

- availability of liquidity;
- volatility in the securitization market;
- whole loan sale pricing;
- margin calls by warehouse lenders;
- actual or anticipated fluctuations in our operating results;
- interest rates;
- prepayments on mortgages;
- valuations of securitization related assets;
- cost of funds; and
- general market conditions.

In addition, significant price and volume fluctuations in the stock market have particularly affected the market prices for the common stocks of specialty finance companies such as ours. These broad market fluctuations have adversely affected and may continue to adversely affect the market price of our common stock. If our results of operations fail to meet the expectations of securities analysts or investors in a future quarter, the market price of our common stock could also be materially adversely affected.

Prepayments of Mortgage Loans May Adversely Affect Our Operations

Mortgage prepayments generally increase when fixed mortgage interest rates fall below the then-current interest rates on outstanding adjustable rate mortgage loans. Prepayments on mortgage loans are also affected by the terms and credit grades of the loans and general economic conditions. Most of our adjustable rate mortgages and those backing mortgage-backed securities are originated within six months of the time we purchased the mortgages and generally bear initial interest rates which are lower than their "fully-indexed" amount (the applicable index plus the margin). If we acquire these mortgages at a premium and they are prepaid prior to or soon after the time of adjustment to a fully-indexed rate, we would not have received interest at the fully-indexed rate during such period. This means we would lose the opportunity

to earn interest at that rate over the expected life of the mortgage. Also, if prepayments on our adjustable rate mortgage loans increase when interest rates are declining, our net interest income may decrease if we cannot reinvest the prepayments in mortgage assets bearing comparable rates.

We currently acquire mortgages on a "servicing released" basis, meaning we acquire both the mortgages and the rights to service them. This strategy requires us to pay a higher purchase price or premium for the mortgages. If any mortgage loans that we acquired at a premium are prepaid, generally accepted accounting principles require us to immediately write-off any remaining capitalized premium amount, which would decrease our interest income.

Value of Our Portfolio of Mortgage-Backed Securities May be Adversely Affected

We invest in mortgage-backed securities known as "interest-only," "principal-only," residual interest and subordinated securities. These securities are either created through our own securitizations or those of third parties. Investments in residual interest and subordinated securities are much riskier than investments in senior mortgage-backed securities because these subordinated securities bear all credit losses prior to the related senior securities. On a percentage basis, the risk associated with holding residual interest and subordinated securities is greater than holding the underlying mortgage loans directly due to the concentration of losses in the subordinated securities.

We estimate future cash flows from these securities and value them utilizing assumptions based in part on projected discount rates, mortgage loan prepayments and credit losses. If our actual experience differs from our assumptions we would be required to reduce the value of these securities. The market for our asset-backed securities is extremely limited and we cannot assure you that we could sell these securities at their reported value or at all or that we could recoup our initial investment.

We also bear the risk of loss on any mortgage-backed securities we purchase in the secondary mortgage market. If third parties have been contracted to insure against these types of losses, we would be dependent in part upon the creditworthiness and claims paying ability of the insurer and the timeliness of reimbursement in the event of a default on the underlying obligations. The insurance coverage for various types of losses is limited, and we bear the risk of any losses in excess of the limitation or outside of the insurance coverage.

In addition, we may not obtain our anticipated yield or we may incur losses if the credit support available within certain mortgage-backed securities is inadequate due to unanticipated levels of losses, or due to difficulties experienced by the credit support provider. Delays or difficulties encountered in servicing mortgage-backed securities may cause greater losses and, therefore, greater resort to credit support than was originally anticipated, and may cause a rating agency to downgrade certain classes of our securities.

We Undertake Additional Risks by Acquiring and Investing in Mortgage Loans

Risk of Failure to Obtain Credit Enhancements

We do not obtain credit enhancements such as mortgage pool or special hazard insurance for all of our mortgage loans and investments. Borrowers may obtain private mortgage insurance, but we only require this insurance in limited circumstances. During the time we hold mortgage loans for investment, we are subject to risks of borrower defaults and bankruptcies and special hazard losses that are not covered by standard hazard insurance (such as losses occurring from earthquakes or floods). If a borrower defaults on a mortgage loan that we hold, we bear the risk of loss of principal to the extent there is any deficiency between the value of the related mortgaged property and the amount owing on the mortgage loan. In addition, since defaulted mortgage loans are not considered eligible collateral under our borrowing arrangements, we bear the risk of being required to finance these loans with funds other than borrowed funds until they are ultimately liquidated.

Greater Credit Risks from Non-Conforming Mortgage Loans

Non-conforming residential mortgage loans are residential mortgages that do not qualify for purchase by government sponsored agencies such as the Fannie Mae and Freddie Mac. Our operations may be negatively affected due to our investments in non-conforming loans or securities evidencing interests in such loans. Credit risks associated

with non-conforming mortgage loans are greater than conforming mortgage loans. The interest rates we charge on non-conforming loans are often higher than those charged for conforming loans. The combination of different underwriting criteria and higher rates of interest leads to greater risk including higher prepayment rates and higher delinquency rates and/or credit losses.

Second Mortgages Entail Greater Risks

Our security interest in the property securing second mortgages is subordinated to the interest of the first mortgage holder. If the value of the property is equal to or less than the amount needed to repay the borrower's obligation to the first mortgage holder upon foreclosure, all or a portion of our second mortgage loan will not be repaid.

Geographic Concentration of Mortgage Loans Has Higher Risks

We do not set limitations on the percentage of our mortgage asset portfolio composed of properties located in any one area (whether by state, zip code or other geographic measure). Concentration in any one area increases our exposure to the economic and natural hazard risks associated with that area. We estimate that a high concentration of the loans included in securitizations in which we hold subordinated interests are secured by properties in California. Certain parts of California have experienced an economic downturn in past years and have suffered the effects of certain natural hazards.

Potential Losses Related to Recourse Obligations

Mortgage-backed securities issued in connection with our securitizations have been non-recourse to us, except in the case of a breach of standard representations and warranties made by us when the loans are securitized. While we have recourse against the sellers of mortgage loans, we cannot assure you that they will honor their obligations. We also engaged in bulk whole loan sales pursuant to agreements that provide for recourse by the purchaser against us. In some cases, the remedies available to a purchaser of mortgage loans from us are broader than those available to us against those who sell us these loans. If a purchaser exercises its rights against us, we may not always be able to enforce whatever remedies we may have against our sellers.

We Undertake Additional Risks in Providing Warehouse Financing

As a warehouse lender, we lend money to mortgage bankers on a secured basis and we are subject to the risks associated with lending to mortgage banks, including the risks of fraud, borrower default and bankruptcy, any of which could result in credit losses for us. Our claims as a secured lender in a bankruptcy proceeding may be subject to adjustment and delay.

Value of our Mortgage Servicing Rights is Subject to Adjustment

When we purchase loans that include the associated servicing rights, the allocated cost of the servicing rights is reflected on our financial statements as mortgage servicing rights. To determine the fair value of these servicing rights, we use assumptions to estimate future net servicing income including projected discount rates, mortgage loan prepayments and credit losses. If actual prepayments or defaults with respect to loans serviced occur more quickly than we originally assumed, we would have to reduce the carrying value of our mortgage servicing rights. We do not know if our assumptions will prove correct.

Our Operating Results Will be Affected by the Results of Our Hedging Activities

To offset the risks associated with our conduit operations, we enter into transactions designed to hedge our interest rate risks. To offset the risks associated with our long-term investment operations, we attempt to match the interest rate sensitivities of our adjustable rate mortgage assets held for investment with the associated financing liabilities. Our management determines the nature and quantity of the hedging transactions based on various factors, including market conditions and the expected volume of mortgage loan purchases. We do not limit management's use of certain instruments in such hedging transactions. Although our hedging program currently qualifies for hedge accounting

under generally accepted accounting principles, we cannot assure you that our hedging transactions will offset our risks of loss, and we could incur significant losses.

Reduction in Demand for Residential Mortgage Loans and Our Non-Conforming Loan Products May Adversely Affect Our Operations

The availability of sufficient mortgage loans meeting our criteria is dependent in part upon the size and level of activity in the residential real estate lending market and, in particular, the demand for non-conforming mortgage loans, which is affected by:

- interest rates;
- regional and national economic conditions;
- fluctuations in residential property values; and
- general regulatory and tax developments.

If our mortgage loan purchases decrease, we will have:

- decreased economies of scale;
- higher origination costs per loan;
- reduced fee income;
- smaller gains on the sale of non-conforming mortgage loans; and
- an insufficient volume of loans to effect securitizations which requires us to accumulate loans over a longer period.

Our Delinquency Ratios and Our Performance May be Adversely Affected by the Performance of Parties Who Sub-Service our Loans

We contract with third-party sub-servicers for the sub-servicing of all our loans, including those in our securitizations, and our operations are subject to risks associated with inadequate or untimely servicing. Poor performance by a sub-servicer may result in greater than expected delinquencies and losses on our loans. A substantial increase in our delinquency or foreclosure rate could adversely affect our ability to access the capital and secondary markets for our financing needs. Also, with respect to loans subject to a securitization, greater delinquencies would adversely impact the value of any "interest-only," "principal-only" and subordinated securities we hold in connection with that securitization.

In a securitization, relevant agreements permit us to be terminated as servicer under specific conditions described in these agreements, such as the failure of a sub-servicer to perform certain functions within specific time periods. If, as a result of a sub-servicer's failure to perform adequately, we were terminated as servicer of a securitization, the value of any servicing rights held by us would be adversely impacted.

Intense Competition for Mortgage Loans May Adversely Affect Our Operations

We compete in purchasing non-conforming mortgage loans and issuing mortgage-backed securities with:

- other mortgage conduit programs;
- investment banking firms;
- savings and loan associations;
- banks;
- thrift and loan associations;
- finance companies;
- mortgage bankers;
- insurance companies;
- other lenders; and
- other entities purchasing mortgage assets.

Continued consolidation in the mortgage banking industry may adversely affect us by reducing the number of current sellers to our conduit operations and our potential customer base. As a result, we may have to purchase a larger percentage of mortgage loans from a smaller number of sellers which could cause us to have to pay higher premiums for loans.

If We Fail to Maintain Our REIT Status We May be Subject to Taxation as a Regular Corporation

Consequences if We Fail to Qualify as a REIT

We believe that we have operated and intend to continue to operate in a manner that enables us to meet the requirements for qualification as a REIT for Federal income tax purposes. We have not requested, and do not plan to request, a ruling from the Internal Revenue Service that we qualify as a REIT.

You should be aware that opinions of counsel are not binding on the IRS or any court. Moreover, no assurance can be given that legislation, new regulations, administrative interpretations or court decisions will not significantly change the tax laws with respect to qualification as a REIT or the federal income tax consequences of such qualification. Both the validity of the opinion of counsel and our continued qualification as a REIT will depend on our satisfaction of certain asset, income, organizational and stockholder ownership requirements on a continuing basis.

If we fail to qualify as a REIT, we would not be allowed a deduction for distributions to stockholders in computing our taxable income and would be subject to Federal income tax at regular corporate rates. We also could be subject to the Federal alternative minimum tax. Unless we are entitled to relief under specific statutory provisions, we could not elect to be taxed as a REIT for four taxable years following the year during which we were disqualified. Therefore, if we lose our REIT status, the funds available for distribution to you would be reduced substantially for each of the years involved.

Effect of Distribution Requirements

As a REIT, we are subject to annual distribution requirements, which limit the amount of cash we have available for other business purposes, including amounts to fund our growth.

Other Tax Liabilities

Even if we qualify as a REIT, we may be subject to certain Federal, state, and local taxes on our income, property and operations that could reduce operating cash flow.

Recent Developments

The Tax Relief Extension Act of 1999 was recently enacted and it contains several tax provisions regarding REITs. It includes a provision which reduces the annual distribution requirement for REIT taxable income from 95% to 90%. It also changes the 10% voting securities test under current law to a 10% vote or value test. Thus, subject to certain exceptions, a REIT will no longer be allowed to own more than 10% of the vote or value of the outstanding securities of any issuer, other than a qualified REIT subsidiary or another REIT. One exception to this new test, which is also an exception to the 5% asset test under current law, allows a REIT to own any or all of the securities of a "taxable REIT subsidiary." A taxable REIT subsidiary can perform non-customary services as well as engage in non-real estate activities. A taxable REIT subsidiary will be taxed as a regular C corporation but will be subject to earnings stripping limitations on the deductibility of interest paid to its REIT. In addition, the REIT will be subject to a 100% excise tax to the extent any transaction between the taxable REIT subsidiary and the REIT is not conducted on an arm's length basis securities of a taxable REIT subsidiary will constitute non-real-estate assets for purposes of determining whether at least 75% of a REIT's assets consist of real estate assets. In addition, no more that 20% of a REIT's total assets can consist of securities of taxable REIT subsidiaries. These new tax provisions are not effective until January 1, 2001. In addition, grandfather protection is provided with respect to the 10% value test for securities of a corporation held by a REIT on July 12, 1999, but such protection ceases to apply after the corporation engages in a substantial new line of business or acquires any substantial asset and also ceases to apply after the acquisition of additional securities of the corporation by the REIT after July 12, 1999.

Because we currently own more than 10% of the value of IFC, we may have to restructure the ownership of IFC or have it elect to be a taxable REIT subsidiary of the Company in 2001.

Potential Characterization of Distributions or Gain on Sale as Unrelated Business Taxable Income to Tax-Exempt Investors

If (1) we are subject to the rules relating to taxable mortgage pools or we are a "pension-held REIT," or (2) a tax-exempt stockholder has incurred debt to purchase or hold our common stock is not exempt from Federal income taxation under certain special sections of the Internal Revenue Code, or (3) the residual REMIC interests we buy generate "excess inclusion income," then distributions to and, in the case of a stockholder described in (2), gains realized on the sale of common stock by, such tax-exempt stockholder may be subject to Federal income tax as unrelated business taxable income under the Internal Revenue Code.

Classification as a Taxable Mortgage Pool Could Subject Us to Increased Taxation

If we have borrowings with two or more maturities and, (1) are secured by mortgage loans or mortgage-backed securities and, (2) the payments made on the borrowings are related to the payments received on the underlying assets, then the borrowings may be classified as a "taxable mortgage pool" under the Internal Revenue Code. If any part of our company was treated as a taxable mortgage pool, then our REIT status would not be impaired, but a portion of the taxable income we generated may, under regulations to be issued by the Treasury Department, be characterized as "excess inclusion" income and allocated to our stockholders. Any excess inclusion income would:

- not be allowed to be offset by a stockholder's net operating losses;
- be subject to a tax as unrelated business income if a stockholder were a tax-exempt stockholder;
- be subject to the application of federal income tax withholding at the maximum rate (without reduction for any otherwise applicable income tax treaty) with respect to amounts allocable to foreign stockholders; and
- be taxable (at the highest corporate tax rate) to us, rather than to our stockholders, to the extent the excess inclusion income relates to stock held by disqualified organizations (generally, tax-exempt companies not subject to tax on unrelated business income, including governmental organizations).

We take the position that our existing financing arrangements do not create a taxable mortgage pool. However, the IRS may successfully maintain that our financing arrangements do qualify as a taxable mortgage pool. In addition, we may enter into arrangements creating excess inclusion income in the future.

Our Operations May be Adversely Affected if We are Subject to the Investment Company Act

We intend to conduct our business at all times so as not to become regulated as an investment company under the Investment Company Act. The Investment Company Act exempts entities that are primarily engaged in the business of purchasing or otherwise acquiring mortgages and other liens on and interests in real estate. In order to qualify for this exemption we must maintain at least 55% of our assets directly in mortgage loans, qualifying pass-through certificates and certain other qualifying interests in real estate. Our ownership of certain mortgage assets may be limited by the provisions of the Investment Company Act. If the Securities and Exchange Commission adopts a contrary interpretation with respect to these securities or otherwise believes we do not satisfy the above exception, we could be required to restructure our activities or sell certain of our assets. To insure that we continue to qualify for the exemption we may be required at times to adopt less efficient methods of financing certain of our mortgage assets and we may be precluded from acquiring certain types of higher-yielding mortgage assets. The net effect of these factors will be to lower at times our net interest income. If we fail to qualify for exemption from registration as an investment company, our ability to use leverage would be substantially reduced, and we would not be able to conduct our business as described. Our business will be materially and adversely affected if we fail to qualify for this exemption.

Future Revisions in Policies and Strategies at the Discretion of Our Board of Directors May be Affected Without Stockholder Consent

Our board of directors, including a majority of our unaffiliated directors, has established our investment and operating policies and strategies. We may:

- invest in the securities of other REITs for the purpose of exercising control;
- offer securities in exchange for property; and
- offer to repurchase or otherwise reacquire our shares or other securities in the future.

In October 1998, we adopted a repurchase plan to repurchase up to $5.0 million of our common stock in the open market. In September 1999, the board of directors approved common stock repurchases up to an additional $5.0 million, or a total of $10.0 million. As of December 31, 1999, we had repurchased 2.0 million shares for $9.9 million. We may also underwrite the securities of other issuers, although we have no present intention to do so. Any of the policies, strategies and activities may be modified or waived by our board of directors, subject in certain cases to approval by a majority of our unaffiliated directors, without stockholder consent.

Effect of Future Offerings May Adversely Affect Market Price of Our Securities

We intend to increase our capital resources by making additional private or public offerings of securities in the future. We do not know:

- the actual or perceived effect of these offerings;
- the timing of these offerings;
- the dilution of the book value or earnings per share of our securities then outstanding; and
- the effect on the market price of our securities then outstanding.

Risk Relating to Common Stock

The sale or the proposed sale of substantial amounts of our common stock in the public market could materially adversely affect the market price of our common stock or other outstanding securities.

Risk Relating to Preferred Stock

Our charter authorizes our board of directors to issue shares of preferred stock and to classify or reclassify any unissued shares of common stock or preferred stock into one or more classes or series of stock. The preferred stock may be issued from time to time with terms as determined by our board of directors. Our preferred stock is available for our possible future financing of acquisitions and for our general corporate purposes without further stockholder authorization. In October 1998, our board announced a dividend to all common stockholders of rights for certain shares of our Series A Junior Preferred Stock. Our Series A Junior Preferred Stock has terms and conditions which could have the effect of delaying, deferring or preventing a hostile change in control of our company. Our board could authorize the issuance of shares of another class or series of preferred stock with terms and conditions which could also have the effect of delaying, deferring or preventing a change in control of our company which could involve a premium price for holders of common stock or otherwise be in their best interest. The preferred stock, if issued, may have a preference on dividend payments, which could reduce the assets we have available to make distributions to our common stockholders.

Maryland Business Combination Statute

The Maryland General Corporation Law establishes special requirements for "business combinations" between a Maryland corporation and "interested stockholders" unless exemptions are applicable. An interested stockholder is any person who beneficially owns 10% or more of the voting power of our then-outstanding voting stock. Among other things, the law prohibits for a period of five years a merger and other similar transactions between our company and an interested stockholder unless the board of directors approved the transaction prior to the party becoming an interested stockholder. The five-year period runs from the most recent date on which the interested stockholder became an

interested stockholder. The law also requires a supermajority stockholder vote for such transactions after the end of the five-year period. This means that the transaction must be approved by at least:

- 80% of the votes entitled to be cast by holders of outstanding voting shares,
- 66% of the votes entitled to be cast by holders of outstanding voting shares other than shares held by the interested stockholder with whom the business combination is to be effected.

The business combination statute could have the effect of discouraging offers to acquire us and of increasing the difficulty of consummating any such offers, even if our acquisition would be in our stockholders' best interests.

Maryland Control Share Acquisition Statute

Maryland law provides that “control shares” of a Maryland corporation acquired in a “control share acquisition” have no voting rights except to the extent approved by a stockholder vote. Two-thirds of the shares eligible to vote must vote in favor of granting the “control shares” voting rights. “Control shares” are shares of stock that, taken together with all other shares of stock the acquirer previously acquired, would entitle the acquirer to exercise at least 20% of the voting power in electing directors. Control shares do not include shares of stock the acquiring person is entitled to vote as a result of having previously obtained stockholder approval. A “control share acquisition” means the acquisition of control shares, subject to certain exceptions.

If a person who has made (or proposes to make) a control share acquisition satisfies certain conditions (including agreeing to pay expenses), he may compel our board of directors to call a special meeting of stockholders to be held within 50 days to consider the voting rights of the shares. If such a person makes no request for a meeting, we have the option to present the question at any stockholders' meeting.

If voting rights are not approved at a meeting of stockholders then we may redeem any or all of the control shares (except those for which voting rights have previously been approved) for fair value. We will determine the fair value of the shares, without regard to voting rights, as of the date of either:

- the last control share acquisition, or
- any meeting where stockholders considered and did not approve voting rights of the control shares.

If voting rights for control shares are approved at a stockholders' meeting and the acquirer becomes entitled to vote a majority of the shares of stock entitled to vote, all other stockholders may exercise appraisal rights. This means that you would be able to force us to redeem your stock for fair value. Under Maryland law, the fair value may not be less than the highest price per share paid in the control share acquisition. Furthermore, certain limitations otherwise applicable to the exercise of dissenters' rights would not apply in the context of a control share acquisition. The control share acquisition statute would not apply to shares acquired in a merger, consolidation or share exchange if we were a party to the transaction. The control share acquisition statute could have the effect of discouraging offers to acquire us and of increasing the difficulty of consummating any such offers, even if our acquisition would be in our stockholders' best interests.

Possible Adverse Consequences of Limits on Ownership of Shares

Our Charter limits ownership of our capital stock by any single stockholder to 9.5% of our outstanding shares. Our Charter also prohibits anyone from buying shares if the purchase would result in us losing our REIT status. This could happen if a share transaction results in fewer than 100 persons owning all of our shares or in five or fewer persons, applying certain broad attribution rules of the Internal Revenue Code, owning 50% or more of our shares. If you or anyone else acquires shares in excess of the ownership limit or in violation of the ownership requirements of the Internal Revenue Code for REITs, we:

- will consider the transfer to be null and void;
- will not reflect the transaction on our books;
- may institute legal action to enjoin the transaction;
- will not pay dividends or other distributions with respect to those shares;

- will not recognize any voting rights for those shares;
- will consider the shares held in trust for the benefit of our Company; and
- will either direct the affected person to sell the shares and turn over any profit to us, or we will redeem the shares. If we redeem the shares, it will be at a price equal to the lesser of:

  (a) the price paid by the transferee of the shares, or
  (b) the average of the last reported sales prices on the American Stock Exchange on the ten trading days immediately preceding the date fixed for redemption by our board of directors.

An individual who acquires shares that violate the above rules bears the risk that (1) he may lose control over the power to dispose of his shares, (2) he may not recognize profit from the sale of his shares if the market price of the shares increases and (3) he may be required to recognize a loss from the sale of his shares if the market price decreases.

Limitations on Acquisition and Change in Control Ownership Limit

The 9.5% ownership limit discussed above may have the effect of precluding acquisition of control of our company by a third party without consent of our board of directors.

ITEM 2. PROPERTIES

The primary executive and administrative offices of the Company are located in Newport Beach, California. The Company has entered into a 10-year lease to use approximately 74,000 square feet of office space at a rate of $149,000 per month. The Company believes that these facilities will adequately provide for the Company's future growth needs.

ITEM 3. LEGAL PROCEEDINGS

The Company is a party to litigation and claims which are normal in the course of its operations. While the results of such litigation and claims cannot be predicted with certainty, the Company believes the final outcome of such matters will not have a materially adverse effect on its results of operations or consolidated financial position.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to the security holders to be voted on during the fourth quarter of 1999.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The Company's Common Stock is listed on the American Stock Exchange ("AMEX") under the symbol IMH. The following table summarizes the high, low and closing sales prices for IMH's Common Stock as reported by the AMEX for the periods indicated:

	1999			1998		
	High	**Low**	**Close**	**High**	**Low**	**Close**
First Quarter	$ 6.19	$ 4.00	$ 5.00	$ 18.25	$ 15.88	$ 17.06
Second Quarter	6.13	4.38	5.06	17.75	14.00	15.56
Third Quarter	6.13	3.88	4.63	16.88	10.00	13.50
Fourth Quarter	4.81	3.38	4.13	13.50	2.75	4.56

On March 14, 2000, the last reported sale price of the Common Stock on the AMEX was $3.31 per share. As of March 14, 2000, there were 671 holders of record (including holders who are nominees for an undetermined number of beneficial owners) of the Company's Common Stock.

Dividend Reinvestment and Stock Purchase Plan. Pursuant to IMH's Dividend Reinvestment and Stock Purchase Plan ("DRSPP" or the "Plan"), stockholders can acquire additional shares of IMH Common Stock by reinvesting their cash dividends at a 0% to 5% discount of the average high and low market prices as reported on the AMEX on the Investment Date (as described in the Plan) to the extent shares are issued by IMH. Stockholders may also purchase additional shares of IMH Common Stock through the cash investment option at a 0% to 5% discount of the average high and low market prices as reported on the AMEX during the three trading days preceding the Investment Date. In July 1999, the Company suspended its DRSPP.

Share Repurchase Program. During 1999, the Company's Board of Directors authorized the Company to repurchase up to $10.0 million of the Company's Common Stock, $.01 par value, in open market purchases from time to time at the discretion of the Company's management; the timing and extent of the repurchases will depend on market conditions. The Company intends to effect such repurchases, if any, in compliance with the Rule 10b-18 under the Securities Exchange Act of 1934. For the year ended December 31, 1999, the Company repurchased 2.0 million shares of its Common Stock for $9.9 million. The acquired shares were canceled.

Stockholder Rights Plan. On October 7, 1998, the Company's Board of Directors adopted a Stockholder Rights Plan in which Preferred Stock Purchase Rights were distributed as a dividend at the rate of one Right for each outstanding share of Common Stock. The dividend distribution was made on October 19, 1998 payable to stockholders of record on that date. The Rights are attached to the Company's Common Stock. The Rights will be exercisable and trade separately only in the event that a person or group acquires or announces the intent to acquire 10 percent or more of the Company's Common Stock. Each Right will entitle stockholders to buy one-hundredth of a share of a new series of junior participating Preferred Stock at an exercise price of $30.00. If the Company is acquired in a merger or other transaction after a person has acquired 10 percent or more of Company outstanding Common Stock, each Right will entitle the stockholder to purchase, at the Right's then-current exercise price, a number of the acquiring Company's common shares having a market value of twice such price. In addition, if a person or group acquires 10 percent or more of the Company's Common Stock, each Right will entitle the stockholder (other than the acquiring person) to purchase, at the Right's then-current exercise price, a number of shares of the Company's Common Stock having a market value of twice such price. Following the acquisition by a person of 10 percent or more of the Company's Common Stock and before an acquisition of 50 percent or more of the Common Stock, the Board of Directors may exchange the Rights (other than the Rights owned by such person) at an exchange ratio of one share of Common Stock per Right. Before a person or group acquires beneficial ownership of 10 percent or more of the Company's Common Stock, the Rights are redeemable for $.0001 per right at the option of the Board of Directors. The Rights will expire on October 19, 2008. The Rights distribution is not taxable to stockholders. The Rights are intended to enable all the Company stockholders to realize the long-term value of their investment in the Company.

Dividends

To maintain its qualification as a REIT, IMH intends to make annual distributions to stockholders of at least 95% of its taxable income, which may not necessarily equal net income as calculated in accordance with generally accepted accounting principles ("GAAP"), determined without regard to the deduction for dividends paid and excluding any net capital gains. Any taxable income remaining after the distribution of the regular quarterly or other dividends will be distributed annually on or prior to the date of the first regular quarterly dividend payment date of the following taxable year. The dividend policy is subject to revision at the discretion of the Board of Directors. All distributions in excess of those required for IMH to maintain REIT status will be made by IMH at the discretion of the Board of Directors and will depend on the taxable earnings of IMH, the financial condition of IMH, and such other factors as the Board of Directors deems relevant. The Board of Directors has not established a minimum distribution level.

Distributions to stockholders will generally be taxable as ordinary income, although a portion of such distributions may be designated by IMH as capital gain or may constitute a tax-free return of capital. IMH annually furnishes to each of its stockholders a statement setting forth distributions paid during the preceding year and their characterization as ordinary income, capital gains or return of capital. Of the total dividends paid during 1999 and 1998, approximately $4.8 million and $8.9 million, respectively, represented a tax-free return of capital.

The following table summarizes dividends paid or declared by IMH:

Period Covered	Stockholder Record Date	Per Share Dividend Amount (1)
Quarter ended March 31, 1998	April 9, 1998	$0.48
Quarter ended June 30, 1998	July 1, 1998	$0.49
Quarter ended September 30, 1998 (1)	October 9, 1998	$0.49
Quarter ended March 31, 1999	April 9, 1999	$0.10
Quarter ended June 30, 1999	June 30, 1999	$0.12
Quarter ended September 30, 1999	September 30, 1999	$0.13
Quarter ended December 31, 1999	January 3, 2000	$0.13

(1) On September 28, 1998, the Company declared a third quarter dividend of $0.49 per share payable on October 26, 1998 to stockholders of record on October 9, 1998. However, on October 8, 1998 the Company announced that the third quarter dividend would be delayed and paid on January 6, 1999. The Company paid interest in the form of an additional cash dividend at a rate of 4% per annum for the period from the previously announced payment date through January 6, 1999. The total amount of interest paid was $96,300, or $0.004 per share.

The Company did not declare a dividend for the quarter ended December 31, 1998. See "Item 1. Business—Risk Factors—Inability to Generate Liquidity May Adversely Affect Our Operations."

ITEM 6. SELECTED CONSOLIDATED FINANCIAL DATA

The following selected consolidated statements of operations data for each of the years in the five-year period ended December 31, 1999, and the consolidated balance sheet data for the five-year period ended December 31, 1999 were derived from the Company's and IFC's financial statements audited by KPMG LLP ("KPMG"), independent auditors, whose reports appear on pages F-2 and F-32, respectively. Such selected financial data should be read in conjunction with the consolidated financial statements and the notes to the consolidated financial statements starting on page F-1 and with Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations."

IMPAC MORTGAGE HOLDINGS, INC.
(dollar amounts in thousands, except per share data)

	Year Ended December 31,				
	1999	1998	1997	1996	1995
Statement of Operations Data:					
Net interest income:					
Total interest income	$ 119,458	$ 163,658	$ 109,533	$ 63,673	$ 2,851
Total interest expense	89,795	121,695	76,577	44,144	1,715
Net interest income	29,663	41,963	32,956	19,529	1,136
Provision for loan losses	5,547	4,361	6,843	4,350	488
Net interest income after loan loss provision	24,116	37,602	26,113	15,179	648
Non-interest income:					
Equity in net earnings (loss) of IFC	4,292	(13,876)	8,316	903	1,489
Equity in net loss of ICH	—	(998)	(239)	—	—
Loss on sale of mortgage loans	—	(3,111)	—	—	—
Gain on sale of securities	93	427	648	—	—
Other income	2,517	4,019	1,601	593	244
Total non-interest income	6,902	(13,539)	10,326	1,496	1,733
Non-interest expense:					
Write-down on securities available-for-sale	2,037	14,132	—	—	—
Loss on equity investment of ICH	—	9,076	—	—	—
General and administrative and other operating expense	6,664	6,788	1,851	1,449	209
Advisory fees	—	—	6,242	3,347	38
Termination agreement expense	—	—	44,375	—	—
Total non-interest expense	8,701	29,996	52,468	4,796	247
Earnings (loss) before income taxes	22,317	(5,933)	(16,029)	11,879	2,134
Income taxes (benefit)	—	—	—	—	76
Net earnings (loss)	$ 22,317	$ (5,933)	$ (16,029)	$ 11,879	$ 2,058
Net earnings (loss) per share— basic	$ 0.83	$ (0.25)	$ (0.99)	$ 1.34	$ 0.05
Net earnings (loss) per share— diluted	$ 0.76	$ (0.25)	$ (0.99)	$ 1.32	$ 0.05
Dividends declared per share	$ 0.48	$ 1.46	$ 1.68	$ 1.61	$ —
Net earnings (loss) per share before Management termination expense (1)	$ 0.76	$ (0.25)	$ 1.74	$ 1.32	$ 0.05

(1) Per share amounts exclude the effect of expenses related to the termination in December 1997 (the "Termination Agreement Expense") of the Company's Management Agreement with Imperial Credit Advisors, Inc. ("ICAI"), an affiliate of ICII.

	At December 31,				
	1999	1998	1997	1996	1995
Balance Sheet Data:					
Investment securities available-for-sale	$ 93,206	$ 93,486	$ 67,011	$ 63,506	$ 2,284
Mortgage loans held-for-investment and CMO collateral	1,313,112	1,181,847	1,052,610	502,658	—
Finance receivables	197,119	311,571	533,101	362,312	583,021
Investment in Impac Funding Corporation	17,372	13,246	27,122	9,896	866
Investment in Impac Commercial Holdings, Inc.	—	—	17,985	—	—
Total assets	1,675,430	1,665,504	1,752,812	972,355	613,688
CMO borrowings	850,817	1,072,316	741,907	474,513	—
Reverse repurchase agreements	539,687	323,625	755,559	357,716	567,727
Total liabilities	1,436,586	1,413,898	1,523,782	843,165	568,452
Total stockholders' equity	238,844	251,606	229,030	129,190	45,236

IMPAC FUNDING CORPORATION
(dollar amounts in thousands, except Operating Data)

	Year Ended December 31,				
	1999	1998	1997	1996	1995
Statement of Operations Data:					
Net interest income:					
Total interest income	$ 21,225	$ 48,510	$ 48,020	$ 32,799	$ 1,249
Total interest expense	20,953	40,743	41,628	31,751	1,785
Net interest income (expense)	272	7,767	6,392	1,048	(536)
Non-interest income:					
Gain (loss) on sale of loans	27,098	(11,663)	19,414	7,747	4,135
Mark-to-market loss on investment securities	—	(805)	—	—	—
Gain (loss) on sale of investment securities	—	(706)	550	—	—
Loan servicing income	5,221	7,071	4,109	1,250	5,159
Gain on sale of servicing rights	—	—	—	—	370
Other income	979	420	93	—	—
Total non-interest income	33,298	(5,683)	24,166	8,997	9,664
Non-interest expense:					
General and administrative and other operating expense	14,965	14,385	10,047	7,154	3,663
Amortization of mortgage servicing rights	5,331	6,361	2,827	613	2,892
Write down of securities available-for-sale	4,252	—	—	—	—
Impairment of mortgage servicing rights	1,078	3,722	—	—	—
Provision for repurchases	385	367	3,148	687	—
Total non-interest expense	26,011	24,835	16,022	8,454	6,555
Earnings (loss) before income taxes	7,559	(22,751)	14,536	1,591	2,573
Income taxes (benefit)	3,227	(8,738)	6,136	679	1,069
Net earnings (loss)	$ 4,332	$ (14,013)	$ 8,400	$ 912	$ 1,504

	At December 31,				
	1999	1998	1997	1996	1995
Balance Sheet Data:					
Residual interests in securitizations	$ —	$ —	$ —	$ 46,949	$ —
Mortgage loans held-for-sale	68,084	252,568	620,549	334,104	544,275
Mortgage servicing rights	15,621	14,062	15,568	8,785	—
Total assets	116,246	313,872	656,944	399,171	552,631
Borrowings from IWLG	66,125	192,900	454,840	327,422	550,291
Other borrowings	181	67,058	148,307	—	—
Due to affiliates	14,500	24,382	6,198	54,803	—
Total liabilities	98,698	301,009	629,548	389,175	551,757
Total shareholders' equity	17,548	12,863	27,396	9,996	874
Operating Data (in millions):					
Mortgage loan acquisitions (volume)	$ 1,672	$ 2,249	$ 2,571	$ 1,542	$ 1,133
Master servicing portfolio at period-end	2,879	3,714	3,029	1,550	512
Servicing portfolio at period-end	2,393	3,714	3,029	1,550	512

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Certain information contained in the following Management's Discussion and Analysis of Financial Condition and Results of Operations constitute forward-looking statements within the meaning of the Securities Act of 1933 and the Exchange Act of 1934 which can be identified by the use of forward-looking terminology such as "may," "will," "expect," "intend," "should," "anticipate," "estimate," or "believe" or comparable terminology. The Company's actual results may differ materially from those contained in the forward-looking statements. Factors which may cause such differences to occur are discussed in "Item 1. Business—Risk Factors" as well as those factors discussed below.

General

Impac Mortgage Holdings, Inc. was incorporated in Maryland in August 1995. The Company, together with its subsidiaries and related companies, primarily operates three businesses: (1) the Long-Term Investment Operations, (2) the Conduit Operations, and (3) the Warehouse Lending Operations. The Long-Term Investment Operations invests primarily in non-conforming residential mortgage loans and securities backed by such loans. The Conduit Operations purchases and sells and securitizes primarily non-conforming mortgage loans. The Warehouse Lending Operations provides warehouse and repurchase financing to originators of mortgage loans.

The Company is entitled to 99% of the earnings or losses of IFC through its ownership of all of the non-voting preferred stock of IFC. As such, the Company records its investment in IFC using the equity method. Under this method, original investments are recorded at cost and adjusted by the Company's share of earnings or losses. The Company is a mortgage REIT that elects to be taxed at the corporate level as a REIT for federal income tax purposes, which generally allows the Company to pass through income to stockholders without payment of federal income tax at the corporate level.

Relationships with Impac Entities

On May 5, 1999, Impac Commercial Holdings, Inc. ("ICH") executed a stock purchase agreement pursuant to which it issued to Fortress Partners LP ("Fortress") $12.0 million of series B convertible preferred stock of ICH. In addition, FIC Management Inc. ("FIC"), an affiliate of Fortress, entered into a definitive agreement with RAI Advisors, LLC ("RAI") for the assignment of RAI's rights and interests in the management agreement with ICH. In connection with these transactions, the submanagement agreement among RAI, IMH and IFC was terminated and a new submanagement agreement was entered into among FIC, IMH and IFC and the right of first refusal agreement among RAI, ICH, ICCC, IMH and IFC was terminated. Under the new submanagement agreement, IMH and IFC provide various services including, accounting, data processing and secondary marketing to ICH, as Fortress deems necessary. Messrs. Joseph R. Tomkinson, Chairman and Chief Executive Officer of IMH, and Frank P. Filipps, an unaffiliated director of IMH, remain on the board of directors of ICH.

Many of the officers and directors of the Company are officers, directors and owners of IFC. The Company owns all of the preferred stock of, and 99% of the economic interest in, IFC, while Joseph R. Tomkinson, William S. Ashmore, President and Chief Operating Officer, and Richard J. Johnson, Executive Vice President and Chief Financial Officer, are the holders of all of the outstanding voting stock of, and 1% of the economic interest in, IFC.

Significant Transactions

Common Stock Exchange Offering

In March 1999, certain stockholders of the Company exchanged 1,359,507 shares of their Common Stock, at an average price of $5.70 per share, for 11% senior subordinated debentures due to mature on February 15, 2004. The debentures are unsecured obligations of the Company subordinated to all indebtedness of the Company's subsidiaries. The debentures bear interest at 11% per annum from their date of issuance, payable quarterly, commencing May 15, 1999, until the debentures are paid in full. The debentures mature on February 15, 2004, at which the date may be extended once by the Company to a date not later than May 15, 2004, provided that the Company satisfies certain conditions. Commencing on February 15, 2001, the debentures are redeemable, at the Company's option, in whole at any time or in

part from time to time, at the principal amount to be redeemed plus accrued and unpaid interest thereon to the redemption date.

Exchange of Series B Cumulative Convertible Preferred Stock for Series C Cumulative Convertible Preferred Stock

In February 2000, all shares of Series B 10.5% Cumulative Convertible Preferred Stock ("Series B Preferred Stock") was exchanged for Series C 10.5% Cumulative Convertible Preferred Stock ("Series C Preferred Stock") and the conversion rate was adjusted to $4.72 per share convertible into 5.29661 shares of Common Stock or an aggregate of 6,355,932 shares of Common Stock. Other than the foregoing, the Series C Preferred Stock has the same rights, preferences and privileges as the Series B Preferred Stock.

Collateralized Mortgage Obligations ("CMOs")

The Company issued two CMOs during the year ended December 31, 1999. The first CMO was issued in February 1999 for $183.1 million and was collateralized by $120.8 million of adjustable rate mortgages and $77.8 million of residential loans secured by second trust deeds. The second CMO was issued in June 1999 for $115.0 million and was collateralized by $117.6 million of primarily adjustable rate mortgages. The issuance of CMOs provides the Company with immediate liquidity, a locked-in net interest rate spread and eliminates the Company's exposure to margin calls on such loans.

Real Estate Mortgage Investment Conduits ("REMICs")

The Company issued two REMICs during the year ended December 31, 1999. The first REMIC was issued in September 1999 for $133.2 million and was collateralized by $137.3 million of adjustable rate mortgages. The second REMIC was issued in December 1999 for $226.9 million and was collateralized by $230.1 million of fixed rate mortgages. The REMICs were accounted for as sales of the mortgage loans, which resulted in a gain of $6.5 million.

Definitive Agreement to Acquire a California Thrift and Loan

During the first quarter of 1999, the Company completed a definitive agreement to acquire a California Thrift and Loan ("Bank"). As provided for in the agreement, the Company submitted its application in the second quarter of 1999 for a change of control to the state and federal regulatory agencies for their approval. During the process of reviewing the application, the federal agency raised certain issues. The Company was not able to give the federal agency sufficient comfort with respect to those issues without modifying its proposal. The Company submitted a new application to state and federal regulatory agencies in the first quarter of 2000. The new application was modified from the previous application in several key areas and to more clearly define the Bank as a stand-alone operation that is not reliant upon the Company for its success. It is anticipated that the Bank will market its own unique loan products, which will include mortgages, consumer equity loans and loans on small commercial and multi-family properties. However, there are no assurances that the new application for change of control will be received favorably by either of the state or federal regulatory agencies. In the event that the Company is unsuccessful in its efforts to obtain the Bank charter, management believes that it will have no adverse impact on the future profitability of the Company.

Advance to Impac Funding Corporation

During the second quarter of 1999, IMH advanced to IFC $14.5 million in cash, in exchange for an interest only note at an interest rate of 9.50% with a maturity of June 30, 2004, in anticipation of the initial capitalization of the Bank and to fund the operations of IFC and other strategic opportunities deemed appropriate by IFC.

Business Operations

Business Strategy: During 1999, the Company restructured its balance sheet in order to increase book value per common share, generate additional liquidity and improve overall credit quality of its investment portfolio. The following transactions were completed during 1999: (1) the exchange of 1.4 million shares of Common Stock for 11.0% senior subordinated debt due 2/15/2004, (2) a stock repurchase program to repurchase up 10.0 million shares of outstanding Common Stock and (3) the re-securitization of a portion of its investment securities portfolio. In addition, the Long-Term

Investment Operations acquired from IFC $349.8 million, in unpaid principal balance, of adjustable rate mortgages to be held for long-term investment during the fourth quarter of 1999. During January 2000, the Company completed the issuance of a $460.0 million CMO that was primarily collateralized by the adjustable rate mortgages acquired from IFC during the fourth quarter of 1999.

The exchange of Common Stock for 11.0% senior subordinated debt and the repurchase of outstanding Common Stock during 1999 was accretive to book value by $0.65, or 7%. Book value at December 31, 1999 was $9.76 (calculated assuming liquidation value of the Company's Series B Cumulative Convertible Preferred Stock) as compared to $9.11 on a pro-forma basis. Overall, book value increased 8% to $9.76 at December 31, 1999 as compared to $9.02 at December 31, 1998. Based on the Company's business plan for 2000 and the retention of reported earnings in excess of minimum distribution requirements, the Company expects to increase its book value per share in the future.

The Company completed a re-securitization of a portion of its investment securities available-for-sale in October 1999, which raised additional liquidity for the Company of approximately $23.4 million after repaying short-term borrowings secured by the investment securities portfolio. The cash proceeds were used to acquire mortgages from IFC, increase outstanding lending by the Warehouse Lending Operations, repurchase Common Stock and other business expansion. The Company reduced its reliance on reverse repurchase agreements to finance its investment securities to zero at December 31, 1999 as compared to $24.1 million at December 31, 1998. The Company continued to maintain reduced leverage and strong liquidity levels during the fourth quarter of 1999. The Company's debt-to-equity ratio increased to 6.0:1 at December 31, 1999 as compared to 5.6:1 at December 31, 1998, which was well within the Company's target range.

Throughout 1999, the Company acquired an aggregate of $638.3 million of mortgages from IFC for its Long-Term Investment Operations. These mortgages consisted of $506.6 million, or 79%, of A quality, non-conforming mortgages. Of the $638.3 million of mortgages acquired, $539.7 million, or 85%, were adjustable rate mortgages. In addition, $222.9 million, or 35%, of mortgages acquired during 1999 for long-term investment had prepayment penalties as compared to $147.6 million, or 18%, of mortgages with prepayment penalties acquired during 1998. The Company expects that the higher percentage of mortgages acquired for long-term investment with prepayment penalties will lead to a reduction in overall prepayments. Constant prepayment rates ("CPR") on the Company's CMO portfolio during the fourth quarter of 1999 decreased to 28% CPR as compared to 34% CPR during the fourth quarter of 1998. The loan delinquency rate of mortgages held for long-term investment which were 60 or more days past due, inclusive of foreclosures and delinquent bankruptcies, decreased to 5.43% at December 31, 1999 as compared to 7.58% at December 31, 1998.

The Company's Board of Directors announced a dividend policy for 2000 that allows the Company to expand its business operations and focus on rebuilding the Company's balance sheet without the diluted effect of offering additional shares of Common Stock at current market levels. During 2000, the Company plans to only distribute 100% of taxable earnings. During 1999, the Company paid dividends in excess of taxable earnings, which represented a return of capital to its stockholders, of approximately $4.8 million over minimum distribution requirements. Of the total dividend distributions paid to common stockholders during 1999, 39% represented ordinary income and 61% represented a return of capital.

Long-Term Investment Operations: During the year ended December 31, 1999, the Long-Term Investment Operations, conducted by IMH and IMH Assets, acquired $638.3 million of mortgages from IFC as compared to $866.7 million acquired during 1998. Mortgages purchased by the Long-Term Investment Operations during 1999 consisted of $262,000 of FRMs and $545.2 million of ARMs secured by first liens on residential property and $92.8 million of fixed rate second trust deeds secured by residential property. IMH Assets issued CMOs totaling $298.1 million, which were collateralized by $316.2 million of mortgage loans, during 1999 as compared to CMOs totaling $768.0 million, which were collateralized by $788.2 million of mortgage loans, during 1998. As of December 31, 1999, the Long-Term Investment Operations' portfolio of mortgage loans consisted of $949.7 million of mortgage loans held in trust as collateral for CMOs and $363.4 million of mortgage loans held-for-investment, of which approximately 34% were FRMs and 66% were ARMs. The weighted average coupon of the Long-Term Investment Operations portfolio of mortgage loans was 9.26% at December 31, 1999 with a weighted average margin of 4.37%. The portfolio of mortgage loans included 77% of "A" credit quality, non-conforming mortgage loans and 23% of B/C Loans, as defined by the Company. The Long-Term Investment Operations sold $10.8 million, in unpaid principal balance, of mortgage loans to IFC and none to third party investors as compared to no loan sales to IFC and $73.2 million of loans sold to third party investors during 1998. During 1999, the

Long-Term Investment Operations acquired $22.0 million of securities created by IFC through the issuance of REMICs as compared to $60.6 million during 1998. In addition, the Long-Term Investment Operations had outstanding finance receivables of $197.1 million and investment securities available-for-sale of $93.2 million at December 31, 1999. Of the $93.2 million of investment securities available-for-sale, $56.8 million were subordinated securities collateralized by mortgages, $30.8 million were "interest only" securities, and $5.6 million were subordinated securities collateralized by other loans.

Conduit Operations: The Conduit Operations, conducted by IFC, supports the Long-Term Investment Operations of the Company by supplying IMH and IMH Assets with mortgages for IMH's long-term investment portfolio. As such, IFC sold $638.3 million, in unpaid principal balance, of mortgages to IMH as compared to $866.7 million, in unpaid principal balance, of loans sold during 1998. IFC's mortgage acquisitions decreased 23% to $1.7 billion during 1999 as compared to $2.2 billion of mortgages acquired during 1998. After excluding bulk acquisitions, IFC's acquisitions decreased 11% to $1.6 billion during 1999 as compared to $1.8 billion during 1998. During 1999, IFC securitized $360.1 million, in unpaid principal balance, of mortgages and sold whole loans to third party investors totaling $824.1 million, in unpaid principal balance, of mortgages. This compares to loan securitizations of $907.5 million, in unpaid principal balance, of mortgages and whole loan sales to third party investors of $856.2 million, in unpaid principal balance, of mortgages during 1998. Loan securitizations and sales during 1999 resulted in gain on sale of loans of $27.1 million as compared to loss on sale of loans of $11.7 million during 1998. IFC had deferred revenue of $7.6 million at December 31, 1999 as compared to $10.6 million at December 31, 1998. IFC's master servicing portfolio decreased 22% to $2.9 billion at December 31, 1999 as compared to $3.7 billion at December 31, 1998. Of the $2.9 billion of mortgage loans master serviced by IFC at December 31, 1999, IFC is the master servicer for $1.4 billion of loans collateralizing REMIC securities and $885.2 million of mortgage loans collateralizing CMOs. In addition, of the $2.6 billion of loans master serviced by IFC, IFC owns servicing rights on $2.4 billion in unpaid principal balance of mortgages. Mortgages collateralized by properties located in California represented 40% of IFC's master servicing portfolio at December 31, 1999 and 1998. The loan delinquency rate of mortgages in IFC's master servicing portfolio which were 60 or more days past due, inclusive of foreclosures and delinquent bankruptcies, was 4.37% and 4.82% at December 31, 1999 and 1998, respectively.

Warehouse Lending Operations: At December 31, 1999, the Company, conducted by IWLG, had $1.4 billion of warehouse lines of credit available to 49 borrowers (including IFC), of which $197.1 million was outstanding, including $66.1 million outstanding to IFC, $1.2 million outstanding to ILG and $48,000 outstanding to WSI. James Walsh, Executive Vice President of WSI, is also a Director of IMH.

RESULTS OF OPERATIONS—
IMPAC MORTGAGE HOLDINGS, INC.

Year Ended December 31, 1999 as compared to Year Ended December 31, 1998

Net Earnings (Loss)

Net earnings for the year ended December 31, 1999 of $22.3 million, or $0.76 per diluted common share, compared to a net loss of $(5.9) million, or $(0.25) per diluted common share, for 1998. The loss for 1998 was primarily due to a global liquidity crisis in the mortgage-backed securitization market, which occurred during the latter half of 1998. The deterioration of the mortgage-backed securitization market created liquidity problems as the Company's lenders made margin calls on their repurchase agreements. In order to meet margin calls and reduce borrowings on its outstanding reverse repurchase agreements, the Company sold mortgage loans and mortgage-backed securities at significant losses. In addition, the Company recorded impairment charges on its investment securities available-for-sale and recorded a loss on the sale of its equity investment in ICH. However, as the mortgage-backed securitization market stabilized during 1999, the Company returned to overall profitability, which in large part was due to the profitability on the sale of its mortgage loans at IFC.

Net Interest Income

Net interest income decreased 29% to $29.7 million during 1999 as compared to $42.0 million during 1998. Interest income is primarily interest earned on Mortgage Assets and includes interest income earned on cash and cash equivalents and due from affiliates. Interest expense is primarily interest paid on borrowings on Mortgage Assets and

includes interest expense paid on due to affiliates and senior subordinated debt. Mortgage Assets include CMO collateral, mortgage loans held-for-investment, finance receivables and investment securities available-for-sale. Borrowings on Mortgage Assets include CMO financing, reverse repurchase agreements and borrowings on investment securities available-for-sale. The decrease in net interest income during 1999 as compared to 1998 was primarily the result of lower average Mortgage Assets, which decreased 20% to $1.6 billion during 1999 as compared to $2.0 billion during 1998. Average Mortgage Assets decreased during 1999 as compared to 1998 principally due to the sale of mortgage loans during the fourth quarter of 1998 in order to increase liquidity and meet margin calls. The Company continued to raise liquidity and reduce leverage throughout 1999 as IFC completed monthly whole loan sales on a servicing released basis. As such, the Long-Term Investment Operations' loan acquisitions from IFC decreased 26% to $638.3 million as compared to $866.7 million acquired during 1998. Additionally, due to IFC's decreased loan production and the shorter accumulation and holding period between monthly whole loan sales, average finance receivables to affiliates (primarily IFC) decreased 42% to $232.7 million during 1999 as compared to $403.9 million during 1998. Net interest income also decreased as the net interest margin on Mortgage Assets decreased to 1.84% during 1999 as compared to 2.14% during 1998. The decrease in net interest margin on Mortgage Assets was primarily the result of a decrease in the net interest margin on CMO collateral to 0.79% during 1999 as compared to 1.26% during 1998. The decrease in the net interest margin on CMO collateral during 1999 was primarily due to an increase in amortization of net premiums as a result of higher loan prepayments. CMO collateral significantly affects changes in net interest income as it represents the largest percentage of total Mortgage Assets. Average CMO collateral accounted for 71% of total average Mortgage Assets during 1999 and 63% of total average Mortgage Assets during 1998.

The following table summarizes average balance, interest and weighted average yield on Mortgage Assets and borrowings for the years ended December 31, 1999 and 1998 and includes interest income on Mortgage Assets and interest expense related to borrowings on Mortgage Assets only (dollars in thousands):

	For the year ended December 31, 1999				For the year ended December 31, 1998			
	Average Balance	Interest	Weighted Avg. Yield	% of Portfolio	Average Balance	Interest	Weighted Avg. Yield	% of Portfolio
MORTGAGE ASSETS								
Subordinated securities collateralized by mortgages	$ 87,107	$ 12,604	14.47 %	5.56 %	$ 88,544	$ 11,219	12.67 %	4.47 %
Subordinated securities collateralized by other loans	7,433	834	11.22	0.47	5,364	709	13.22	0.27
Total investment securities available-for-sale	94,540	13,438	14.21	6.03	93,908	11,928	12.70	4.74
Loan receivables:								
CMO collateral	1,119,813	74,096	6.62	71.48	1,244,458	92,011	7.39	62.87
Mortgage loans held-for-investment	34,767	2,345	6.74	2.22	149,131	14,373	9.64	7.54
Finance receivables:								
Affiliated	232,741	19,566	8.41	14.86	403,935	34,166	8.46	20.41
Non-affiliated	84,783	7,779	9.18	5.41	87,855	8,242	9.38	4.44
Total finance receivables	317,524	27,345	8.61	20.27	491,790	42,408	8.62	24.85
Total Loan Receivables	1,472,104	103,786	7.05	93.97	1,885,379	148,792	7.89	95.26
Total Mortgage Assets	$ 1,566,644	$ 117,224	7.48 %	100.00 %	$ 1,979,287	$ 160,720	8.12 %	100.00 %
BORROWINGS								
CMO borrowings	$ 1,017,992	$ 65,212	6.41 %	74.25 %	$ 1,153,985	$ 76,309	6.61 %	64.63 %
Reverse repurchase agreements–mortgages	331,179	21,545	6.51	24.16	605,486	40,439	6.68	33.91
Borrowings secured by securities available-for-sale	6,445	686	10.64	0.47	—	—	—	—
Reverse repurchase agreements–securities	15,377	998	6.49	1.12	26,051	1,700	6.53	1.46
Total Borrowings on Mortgage Assets	$ 1,370,993	$ 88,441	6.45 %	100.00 %	$ 1,785,522	$ 118,448	6.63 %	100.00 %
Net Interest Spread (1)			**1.03 %**				**1.49 %**	
Net Interest Margin (2)			**1.84 %**				**2.14 %**	

(1) Calculated by subtracting the yield on total borrowings on Mortgage Assets from the yield on total Mortgage Assets.

(2) Calculated by subtracting interest on total borrowings on Mortgage Assets from interest on total Mortgage Assets and dividing the result by the average balance of total Mortgage Assets.

Interest income on Mortgage Assets: Interest income on CMO collateral decreased 19% to $74.1 million during 1999 as compared to $92.0 million during 1998 as average CMO collateral decreased 8% to $1.1 billion as compared to $1.2 billion, respectively. Average CMO collateral decreased as the Long-Term Investment Operations issued CMOs totaling $298.1 million during 1999, which were collateralized by $316.2 million of mortgages, as compared to CMOs totaling $768.0 million, which were collateralized by $788.2 million of mortgages, during 1998. Average CMO collateral also decreased due to higher mortgage loan prepayments, which increased 16% to $490.0 million during 1999 as compared to $424.1 million during 1998. CPR on CMO collateral was 37% CPR during 1999 as compared to 30% CPR during 1998. However, $222.9 million, or 35%, of mortgages acquired during 1999 by the Long-Term Investment Operations, had prepayment

penalties as compared to $147.6 million, or 18%, of mortgages acquired with prepayment penalties during 1998. The Company expects that the higher percentage of mortgages acquired for long-term investment with prepayment penalties will lead to a reduction in overall prepayments.

A decrease in the weighted average yield on CMO collateral also contributed to an overall decrease in interest income on CMO collateral during 1999 as compared to 1998. The weighted average yield on CMO collateral decreased to 6.62% during 1999 as compared to 7.39% during 1998. The decrease in yield on CMO collateral during 1999 was primarily due to amortization of net premiums paid in acquiring the mortgage loans held as CMO collateral and a decrease in short-term interest rates, which are used as an index to determine interest rate adjustments on adjustable rate CMO collateral. During 1999, the Company amortized net premiums on CMO collateral of $14.4 million as compared to $11.7 million during 1998. Amortization of net premiums on CMO collateral increased during 1999 as compared to 1998 primarily due to the increase in the CPR, as previously mentioned. However, during 1999 IFC limited premiums paid on loans without prepayment penalties. During 1999, IFC acquired mortgage loans at a weighted average price paid of 101.5 as compared to a weighted average price paid of 102.3 during 1998. As of December 31, 1999, net premiums on CMO collateral was $28.8 million as compared to $39.4 million at December 31, 1998.

Interest income on mortgage loans held-for-investment decreased 84% to $2.3 million during 1999 as compared to $14.4 million during 1998 as average mortgage loans held-for-investment decreased 77% to $34.8 million as compared to $149.1 million, respectively. Average mortgage loans held-for-investment decreased due to a decrease in mortgage loan acquisitions by the Long-Term Investment Operations during 1999 as compared to 1998. Mortgage loans acquired from IFC by the Long-Term Investment Operations decreased 26% to $638.3 million as compared to $866.7 million acquired during 1998. As the Company focused on increased liquidity and reduced leverage during 1999, the Long-Term Investment Operations reduced its acquisition of mortgage loans to be held for long-term investment and concentrated on selling mortgage loans at IFC. Additionally, the decrease in the weighted average yield on mortgage loans held-for-investment during 1999 as compared to 1998 contributed to the decrease in interest income. The weighted average yield decreased to 6.74% during 1999 as compared to 9.64% during 1998. The decrease in the yield on mortgage loans held-for-investment during 1999 was primarily due to the sale of high-yielding 125 Loans by the Long-Term Investment Operations to IFC in December of 1998 and a decrease in mortgage rates during 1999. The majority of 125 Loans that were held by the Long-Term Investment Operations were sold to IFC. Interest income on mortgage loans held-for-investment includes the effect of amortization of net premiums paid in acquiring the mortgage loans. As of December 31, 1999, net premiums on mortgage loans held-for-investment was $2.0 million as compared to $482,000 as of December 31, 1998.

Interest income on finance receivables decreased 36% to $27.3 million during 1999 as compared to $42.4 million during 1998 as average finance receivables decreased 35% to $317.5 million as compared to $491.8 million, respectively. The decrease in interest income on finance receivables during 1999 was primarily the result of monthly whole loan sales by IFC as compared to quarterly securitizations during 1998 and a decrease in loan acquisitions during 1999 as compared to 1998. IFC's loan accumulation and holding period shortened during 1999 as the Company sought to minimize interest rate and market risk exposure on its mortgage loans held-for-sale and maintain strong liquidity levels through monthly whole loan sales. In addition, IFC's loan acquisitions decreased to $1.7 billion during 1999 as compared to $2.2 billion during 1998. As such, average outstanding finance receivables to affiliates (primarily IFC) decreased to $232.7 million during 1999 as compared to $403.9 million during 1998, which resulted in a decrease in interest income to $19.6 million as compared to $34.2 million, respectively. The weighted average yield on affiliated finance receivables decreased to 8.41% during 1999 as compared to 8.46% during 1998 as the average prime rate, which is the index the Company uses to determine interest rates on finance receivables, was lower during 1999 as compared to 1998. Interest income on finance receivables to non-affiliates decreased 5% to $7.8 million during 1999 as compared to $8.2 million during 1998 as average outstanding finance receivables to non-affiliates decreased to $84.8 million as compared to $87.9 million, respectively. Interest income on finance receivables to non-affiliates also decreased as the weighted average yield decreased to 9.18% during 1999 as compared to 9.38% during 1998 as the average prime rate was lower in 1999 as compared to 1998.

Interest income on investment securities available-for-sale increased 13% to $13.4 million during 1999 as compared to $11.9 million during 1998 as average investment securities increased 1% to $94.5 million as compared to $93.9 million, respectively. Interest income on investment securities primarily increased during 1999 as the weighted average yield on investment securities increased to 14.21% during 1999 as compared to 12.70% during 1998. The yield on investment securities increased during 1999 as compared to 1998 as the Long-Term Investment Operations acquired $18.3 million of

securities from IFC that had a higher weighted average yield than the weighted average yield of the total investment securities portfolio and also due to a change in yield estimates on the remaining securities portfolio.

Interest expense on borrowings: Interest expense on CMO borrowings decreased 15% to $65.2 million during 1999 as compared to $76.3 million during 1998 as average borrowings on CMO collateral decreased 17% to $1.0 billion as compared to $1.2 billion, respectively. Average CMO borrowings decreased as the Long-Term Investment Operations issued CMOs totaling $298.1 million during 1999 as compared to CMOs totaling $768.0 million during 1998. The increase in loan prepayments also contributed to the overall decrease in average CMO borrowings during 1999 as compared to 1998. The weighted average yield of CMO borrowings decreased to 6.41% during 1999 as compared to 6.61% during 1998 as average one-month LIBOR, which is the index used to determine rates on adjustable rate CMO borrowings, was lower during 1999 as compared to 1998. In addition, interest expense on CMO borrowings is affected by the amortization of securitization costs. Securitization costs are incurred when a CMO is issued and securitization costs are capitalized and amortized over the life of the CMO borrowings as an adjustment to the yield. During 1999, the Company amortized securitization costs of $4.2 million as compared to $2.6 million during 1998 due to an increase in loan prepayments during 1999 as compared to 1998. As of December 31, 1999, unamortized securitization costs were $11.9 million as compared to unamortized securitization costs of $12.3 million at December 31, 1998.

Interest expense on reverse repurchase borrowings, which are used to fund the acquisition of mortgage loans and finance receivables, decreased 47% to $21.5 million during 1999 as compared to $40.4 million during 1998 as average reverse repurchase agreements decreased 45% to $331.2 million as compared to $605.5 million, respectively. The decrease in average finance receivables was primarily related to the previously discussed decrease in average finance receivables to IFC. The Warehouse Lending Operations uses reverse repurchase agreements with investment banks to fund its short-term loans to affiliates (primarily IFC) and non-affiliates. As IFC shortened the accumulation and holding period on its mortgage loans held-for-sale and acquired fewer loans during 1999 as compared to 1998, IFC required lower borrowing levels during 1999. The weighted average yield of reverse repurchase agreements collateralized by mortgage loans decreased to 6.51% during 1999 as compared to 6.68% during 1998 as average one-month LIBOR, which is the index used by the Company's lenders to determine interest rates on reverse repurchase borrowings, decreased during 1999 as compared to 1998.

During most of 1999, the Company used investment securities available-for-sale as collateral to borrow under reverse repurchase agreements to fund the purchase of mortgage-backed securities and to act as an additional source of liquidity for the Company's operations. During October 1999, the Company issued notes collateralized by its investment securities available-for-sale to provide a more stable financing source for these assets. Therefore, combined interest expense on reverse repurchase agreements and borrowings secured by investment securities available-for-sale remained unchanged at $1.7 million during 1999 and 1998. The combined average balance on reverse repurchase agreements and borrowings secured by investment securities available-for-sale decreased 16% to $21.8 million as compared to $26.1 million, respectively. The weighted average yield on these combined borrowings increased to 7.72% during 1999 as compared to 6.53% during 1998.

Non-Interest Income

Non-interest income increased to $6.9 million during 1999 as compared to $(13.5) million during 1998. Non-interest income increased primarily due to an increase in equity in net earnings (loss) of IFC. Equity in net earnings (loss) of IFC improved during 1999 as compared to 1998 due to increased profitability from the sale of mortgage loans. In addition, IFC recorded non-cash write-downs on MSRs and investment securities held-for-sale during the fourth quarter of 1998. As discussed previously, loss on loan sales and asset write-downs were due to a deterioration of the mortgage-backed securitization market, which occurred during the latter part of 1998. As the mortgage market stabilized during 1999, IFC returned to overall profitability, which in large part was due to profitability on loan sales.

Equity in Net Earnings (Loss) of IFC

Equity in net earnings (loss) of IFC increased to $4.3 million during 1999 as compared to $(13.9) million during 1998. The Company records 99% of the earnings or losses from IFC, as the Company owns 100% of IFC's preferred stock, which represents 99% of the economic interest in IFC. For more information on the results of operations of IFC, refer to "—Results of Operations—Impac Funding Corporation."

Equity in Net Loss of ICH

The Company's equity in net loss of ICH decreased to zero for 1999 as compared to a loss of $(998,000) for 1998. The Company recorded no earnings or loss from ICH during 1999 as the Company sold its holdings of ICH Common Stock during the fourth quarter of 1998. Prior to the fourth quarter of 1998, the Company recorded equity in net earnings (loss) in ICH by virtue of the Company's ownership of 9.8% of ICH's voting Common Stock and 100% of Class A non-voting Common Stock.

Non-Interest Expense

Non-interest expense decreased to $8.7 million during 1999 as compared to $30.0 million during 1998. Non-interest expense decreased primarily due to a decrease in write-down of investment securities available-for-sale, loss on equity investment and general and administrative and other expense.

Write-down of Investment Securities Available-for-Sale

Write-down of investment securities available-for-sale decreased to $2.0 million during 1999 as compared to $14.1 million during 1998 as the mortgage market recovered from the problems that occurred during the latter half of 1998.

Loss on Equity Investment

Loss on equity investment decreased to zero during 1999 as compared to $9.1 million during 1998 as the Company sold 100% of its Common Stock investment in ICH at a loss during the fourth quarter of 1998.

General and Administrative and Other Expense

General and administrative and other expense decreased to $1.3 million during 1999 as compared to $2.3 million during 1998 as the Company sold its remaining 50% ownership interest in a commercial office building, where the Company maintains its current headquarters, to ICH during the fourth quarter of 1998. Expenses related to the 50% ownership interest in the property decreased to none during 1999 as compared to $622,000 during 1998.

Credit Exposures

Non-performing Assets. Non-performing assets consist of loans that are 90 days or more delinquent ("non-accrual loans"), including loans in foreclosure and delinquent bankruptcies, and real estate acquired in settlement of loans, or other real estate owned. It is the Company's policy to place a mortgage loan on non-accrual status when a loan becomes 90 days delinquent. Any previously accrued interest will be reversed from income. Non-accrual loans are included in mortgage loans held-for-sale at IFC and mortgage loans held-for-investment and CMO collateral at IMH. The outstanding unpaid principal balance of non-performing assets totaled $63.3 million at December 31, 1999 as compared to $80.7 million at December 31, 1998. The decrease in non-performing assets was primarily due to the sale of delinquent mortgage loans held-for-sale at IFC. Of the total non-performing assets at December 31, 1999 and 1998, other real estate owned represented $9.7 million and $9.2 million, respectively, in unpaid principal balance. The carrying amount of other real estate owned, after writing down the mortgage loan to the broker's price opinion or appraised value, was $8.8 million and $8.5 million at December 31, 1999 and 1998, respectively. The Company recorded losses on the disposition of other real estate owned of $2.2 million and $1.7 million during 1999 and 1998, respectively.

The Company monitors its sub-servicers to make sure that they perform loss mitigation, foreclosure and collection functions according to the Company's written policies. This includes an effective and aggressive collection effort in order to minimize mortgage loans from becoming non-performing assets. However, when resolving non-performing assets, the Company's sub-servicers are required to take timely and aggressive action. The sub-servicer is required to determine collectibility under various circumstances, which will result in maximum financial benefit to the Company. This is accomplished by either working with the borrower to bring the loan current or by foreclosing and liquidating the property. The Company performs ongoing reviews of loans that display weaknesses and believes it maintains adequate loss allowances on the mortgage loans.

The following table summarizes the unpaid principal balance of the Company's non-performing assets included in its mortgage loan portfolios for the periods shown (in thousands):

	At December 31,	
	1999	1998
Mortgage Loans Held-for-Sale:		
Non-accrual	$ 2,572	$ 15,328
Other real estate owned	—	—
Total mortgage loans held-for-sale	2,572	15,328
Mortgage Loans Held-for-Investment:		
Non-accrual	8,229	6,870
In process foreclosures	306	1,437
Total mortgage loans held-for-investment	8,535	8,307
CMO collateral:		
Non-accrual	42,792	49,305
Other real estate owned	9,411	7,739
Total CMO collateral	52,203	57,044
Total mortgage loan portfolios	$ 63,310	$ 80,679

Delinquent Loans. When a borrower fails to make required payments on a loan and does not cure the delinquency within 60 days, the Company generally records a notice of default and commences foreclosure proceedings. If the loan is not reinstated within the time permitted by law for reinstatement, the property may then be sold at a foreclosure sale. In foreclosure sales, the Company generally acquires title to the property. At December 31, 1999, loans that were delinquent 30 days or more, as a percentage of the outstanding servicing balance of the mortgage loan portfolios, was 10.98% as compared to 12.80% at December 31, 1998.

The following table summarizes the unpaid principal balance of the Company's delinquent mortgage loans included in its mortgage loan portfolios for the periods shown (in thousands):

	At December 31,	
	1999	1998
Mortgage Loans Held-for-Sale:		
30-59 days delinquent	$ 9,140	$ 6,976
60-89 days delinquent	1,838	1,448
90 or more days delinquent (1)	2,572	15,328
Total mortgage loans held-for-sale	13,550	23,752
Mortgage Loans Held-for-Investment:		
30-59 days delinquent	7,029	2,384
60-89 days delinquent	1,453	271
90 or more days delinquent (1)	8,229	6,870
Total mortgage loans held-for-investment	16,711	9,525
CMO collateral:		
30-59 days delinquent	50,822	63,953
60-89 days delinquent	12,398	18,695
90 or more days delinquent (1)	42,792	49,305
Total CMO collateral	106,012	131,953
Total mortgage loan portfolios	$ 136,273	$ 165,230

(1) Includes loans in foreclosure and delinquent bankruptcies.

Provision for Loan Losses. The Company's total allowance for loan losses expressed as a percentage of Gross Loan Receivables which includes loans held-for-investment, CMO collateral and finance receivables, decreased to 0.27% at December 31, 1999 as compared to 0.47% at December 31, 1998. The Company recorded net loan loss provisions of $5.5

million during 1999 as compared to $4.4 million during 1998. The amount provided for loan losses during 1999 increased primarily due to an increase in foreclosures and the subsequent disposition of other real estate owned. The allowance for loan losses is determined primarily on the basis of management's judgment of net loss potential including specific allowances for known impaired loans, changes in the nature and volume of the portfolio, value of the collateral and current economic conditions that may affect the borrowers' ability to pay.

Year Ended December 31, 1998 as compared to Year Ended December 31, 1997

Net Earnings (Loss)

The Company recorded a net loss of $(5.9) million, or $(0.25) per basic and diluted common share, during the year ended December 31, 1998 as compared to a net loss of $(16.0) million, or $(0.99) per basic and diluted common share, for the year ended December 31, 1997. The Company's net loss for 1998 was primarily the result of a tax adjusted loss of $7.3 million on the sale of mortgage loans held-for-sale at IFC and a tax adjusted non-cash charge of $2.9 million on the write-down of IFC's MSRs and investment securities available-for-sale. In addition, the Company's 1998 earnings were negatively affected by a $9.1 million loss on the sale of its equity investment in ICH, which reflects the price the Company received on the sale of its ICH common stock on October 19, 1998, an impairment charge of $14.1 million on investment securities available-for-sale, a loss on sale of mortgage loans of $3.1 million, and a loss on disposition of real estate owned of $1.7 million. Excluding the consolidated tax adjusted losses on mortgage loan sales of $10.4 million, consolidated tax adjusted non-cash charges of $17.0 million, and the loss on sale of equity investment in ICH of $9.1 million, the Company's earnings for the year ended December 31, 1998 would have been $30.6 million, or $1.28 per basic and diluted common share, as compared to earnings of $28.3 million, or $1.74 per basic and diluted common share, for the same period of 1997, after excluding a non-cash charge of $44.4 million for the Company's buyout of its management agreement. Earnings per share for 1998, including the adjustments described above, were lower as compared to earnings per share for 1997 due to an increase in the number of common shares outstanding during 1998.

The loss on the sale of mortgage loans and the write-down of mortgage assets by the Company and IFC was precipitated by the deterioration of the mortgage-backed securitization market during the third and fourth quarters of 1998. The deterioration of the mortgage-backed securitization market in 1998 created liquidity problems for the Company as the Company's lenders made margin calls on their reverse repurchase facilities. These margin calls resulted in the Company delaying its third quarter dividend, which was paid on January 6, 1999, and selling mortgage loans and mortgage-backed securities at losses in order to reduce outstanding borrowings on these facilities. Although a loss was recorded for 1998, the Company was successful in improving liquidity and protecting stockholder value by selling out of its mortgage loan positions rather than continuing to expose the Company to further market risk while accumulating these loans for securitization.

Net Interest Income

Net interest income increased 27% to $42.0 million during 1998 as compared to $33.0 million during 1997. Interest income is primarily interest earned on Mortgage Assets and includes interest income earned on cash and cash equivalents and due from affiliates. Interest expense is primarily interest paid on borrowings on Mortgage Assets and includes interest expense paid on due to affiliates. Mortgage Assets include CMO collateral, mortgage loans held-for-investment, finance receivables and investment securities available-for-sale. Borrowings on Mortgage Assets include CMO borrowings and reverse repurchase agreements. The increase in net interest income during 1998 as compared to 1997 was primarily the result of higher average Mortgage Assets, which increased 54% to $2.0 billion during 1998 as compared to $1.3 billion during 1997. The net interest spread on Mortgage Assets decreased to 1.49% during 1998 as compared to 1.89% during 1997. The decrease in net interest spread on Mortgage Assets was primarily the result of a decrease in the net interest spread on CMO collateral, which represents the largest portion of Mortgage Assets on a weighted-average basis. The net interest spread on CMO collateral was 0.78% during 1998 as compared to 1.40% during 1997. The decrease in net interest spread on CMO collateral during 1998 was primarily due to higher rates of mortgage loan prepayments and correspondingly higher rates of premium amortization expense as compared to 1997.

The following table summarizes average balance, interest and weighted-average yield on Mortgage Assets and borrowings for the years ended December 31, 1998 and 1997 and includes interest income on Mortgage Assets and interest expense related to borrowings on Mortgage Assets only (dollars in thousands):

	For the year ended December 31, 1998				For the year ended December 31, 1997			
	Average Balance	Interest	Weighted Avg. Yield	% of Portfolio	Average Balance	Interest	Weighted Avg. Yield	% of Portfolio
MORTGAGE ASSETS								
Subordinated securities collateralized by mortgages	$ 88,544	$ 11,219	12.67 %	4.47 %	$ 58,956	$ 7,519	12.75 %	4.51 %
Subordinated securities collateralized by other loans	5,364	709	13.22	0.27	5,980	1,028	17.19	0.46
Total investment securities available-for-sale	93,908	11,928	12.70	4.74	64,936	8,547	13.16	4.97
Loan receivables:								
CMO collateral	1,244,458	92,011	7.39	62.87	626,831	47,967	7.65	47.93
Mortgage loans held-for-investment	149,131	14,373	9.64	7.54	182,215	14,535	7.98	13.93
Finance receivables:								
Affiliated	403,935	34,166	8.46	20.41	403,931	34,299	8.49	30.88
Non-affiliated	87,855	8,242	9.38	4.44	29,963	2,991	9.98	2.29
Total finance receivables	491,790	42,408	8.62	24.85	433,894	37,290	8.59	33.17
Total Loan Receivables	1,885,379	148,792	7.89	95.26	1,242,940	99,792	8.03	95.03
Total Mortgage Assets	$ 1,979,287	$ 160,720	8.12 %	100.0 %	$ 1,307,876	$ 108,339	8.28 %	100.00 %
BORROWINGS								
CMO borrowings	$ 1,153,985	$ 76,309	6.61 %	64.63 %	$ 586,463	$ 36,665	6.25 %	49.06 %
Reverse repurchase agreements–mortgages	605,486	40,439	6.68	33.91	580,908	37,881	6.52	48.59
Reverse repurchase agreements–securities	26,051	1,700	6.53	1.46	28,109	1,836	6.53	2.35
Total Borrowings on Mortgage Assets	$ 1,785,522	$ 118,448	6.63 %	100.00 %	$ 1,195,480	$ 76,382	6.39 %	100.00 %
Net Interest Spread			**1.49 %**				**1.89 %**	
Net Interest Margin			**2.14 %**				**2.44 %**	

Interest income on Mortgage Assets: Interest income on CMO collateral increased 92% to $92.0 million during 1998 as compared to $48.0 million during 1997 as average CMO collateral increased 91% to $1.2 billion as compared to $626.8 million, respectively. Average CMO collateral increased as the Long-Term Investment Operations issued CMOs totaling $768.0 million during 1998, which were collateralized by $788.2 million of mortgages held by the Long-Term Investment Operations. The weighted average yield on CMO collateral decreased to 7.39% during 1998 as compared to 7.65% during 1997. The decrease in the yield on CMO collateral during 1998 was primarily due to higher rates of mortgage loan prepayments and correspondingly higher rates of premium amortization expense as compared to 1997. Interest income on CMO collateral includes the effect of amortization of net premiums paid in acquiring the mortgage loans. As of December 31, 1998, net premiums on CMO collateral was $39.4 million.

Interest income on mortgage loans held-for-investment decreased 1% to $14.4 million during 1998 as compared to $14.5 million during 1997 as average mortgage loans held-for-investment decreased 18% to $149.1 million as compared to $182.2 million, respectively. The weighted average yield on mortgage loans held-for-investment increased to 9.64% during 1998 as compared to 7.98% during 1997. The increase in the yield on mortgage loans held-for-investment during 1998 was primarily due to higher average balance of 125 Loans outstanding and held in portfolio during 1998 as

compared to 1997. Most of the 125 Loans that were held by the Long-Term Investment Operations were sold to IFC in December 1998. Interest income on mortgage loans held-for-investment includes the effect of amortization of net premiums paid in acquiring the mortgage loans. As of December 31, 1998, net premiums on mortgage loans held-for-investment was $482,000.

Interest income on finance receivables increased 14% to $42.4 million during 1998 as compared to $37.3 million during 1997 as average finance receivables increased 13% to $491.8 million as compared to $433.9 million, respectively. The increase in interest income on finance receivables was primarily the result of an increase of 193% in average finance receivables to non-affiliated mortgage banking companies to $87.9 million during 1998 as compared to $30.0 million during 1997. Interest income on finance receivables to non-affiliates increased 173% to $8.2 million during 1998 as compared to $3.0 million during 1997. The weighted average yield on non-affiliated finance receivables decreased to 9.38% during 1998 as compared to 9.98% during 1997. Average finance receivables outstanding to affiliates was constant at $403.9 million during 1998 and 1997. Interest income on finance receivables to affiliates decreased to $34.2 million during 1998 as compared to $34.3 million during 1997. The weighted average yield on affiliated finance receivables decreased to 846% during 1998 as compared to 8.49% during 1997. The overall weighted average yield on finance receivables increased to 8.62% during 1998 as compared to 8.59% during 1997.

Interest income on investment securities available-for-sale increased 40% to $11.9 million during 1998 as compared to $8.5 million during 1997 as average investment securities available-for-sale increased 45% to $93.9 million as compared to $64.9 million, respectively. The increase in average securities available-for-sale during 1998 was the result of the Long-Term Investment Operations purchasing and retaining mortgage-backed securities of $60.6 million that were issued by IFC as REMICs. The weighted average yield on investment securities available-for-sale decreased to 12.70% during 1998 as compared to 13.16% during 1997 due to the purchase of lower-yielding securities during 1998.

Interest expense on borrowings: Interest expense on CMO borrowings increased 108% to $76.3 million during 1998 as compared to $36.7 million during 1997 as average borrowings on CMO collateral increased 105% to $1.2 billion as compared to $586.5 million, respectively. Average CMO borrowings increased as the Long-Term Investment Operations issued CMOs totaling $768.0 million during 1998. The weighted average yield of CMO borrowings increased to 6.61% during 1998 as compared to 6.25% during 1997. This increase was the result of the Company issuing fixed-rate CMOs totaling $583.0 million during 1998 at higher interest rates than the initial interest rates on variable-rate CMOs the Company issued prior to 1998. Although borrowing rates on the fixed-rate CMOs are generally higher than the initial interest rates on variable-rate CMOs, the Company receives a comparable interest rate spread on fixed-rate CMOs as it does on its variable-rate CMOs.

Interest expense on reverse repurchase borrowings used to fund the acquisition of mortgage loans and finance receivables increased 7% to $40.4 million during 1998 as compared to $37.9 million during 1997 as the average balance of reverse repurchase agreements increased 4% to $605.5 million during 1998 as compared to $580.9 million during 1997. The increase in average finance receivables was primarily related to an increase in finance receivables made to non-affiliates of the Company and to the longer time period IFC's mortgage loans were outstanding on IWLG's warehouse facilities during 1998. As the market for mortgage-backed securitizations and whole loan sales deteriorated during the latter half of 1998 and made it more difficult for IFC to securitize or sell mortgage loans, the average number of days that IFC warehoused its mortgage loans with IWLG increased during 1998 as compared to 1997. The weighted average yield of reverse repurchase agreements collateralized by mortgage loans increased to 6.68% during 1998 as compared 6.52% during 1997.

The Company also uses mortgage-backed securities as collateral to borrow under reverse repurchase agreements to fund the purchase of mortgage-backed securities and to act as an additional source of liquidity for the Company's operations. Interest expense on these reverse repurchase agreements decreased 6% to $1.7 million during 1998 as compared to $1.8 million during 1997 as the average balance on these reverse repurchase agreements decreased 7% to $26.1 million as compared to $28.1 million, respectively. The weighted average yield of reverse repurchase agreements collateralized by mortgage-backed securities remained constant at 6.53% during 1998 and 1997.

Non-Interest Income

Equity in Net Earnings (loss) of IFC

The Company's equity in net loss of IFC decreased to a loss of $(13.9) million for 1998 as compared to earnings of $8.3 million for 1997. The decrease in equity in net earnings (loss) of IFC during 1998 was primarily the result of net losses on sale of mortgage loans and non-cash charges for the write-down of MSRs and investment securities available-for-sale. The net loss on sale of mortgage loans and the non-cash charges were due to the deterioration of the mortgage-backed securitization market, as previously discussed. The Company records 99% of the earnings or losses from IFC as the Company owns 100% of IFC's preferred stock, which represents 99% of the economic interest in IFC. For more information on the results of operations of IFC, refer to "—Results of Operations—Impac Funding Corporation."

Equity in Net Loss of ICH

The Company's equity in net loss of ICH increased to a loss of $(998,000) for 1998 as compared to a loss of $(239,000) for 1997. The increase in equity in net loss of ICH during 1998 was primarily the result of a deficit in equity in net earnings (loss) of ICCC of $(19.2), which ICH records on its consolidated financial statements, and an impairment charge of $1.7 million that ICH recorded on its residual interest in securitization held-for-trading. ICH records 95% of the earnings or losses from ICCC as ICH owns 100% of ICCC's preferred stock, which represents 95% of the economic interest in ICCC. Prior to October 19, 1998, the Company recorded equity in net loss in ICH by virtue of the Company's ownership of 9.8% of ICH's voting Common Stock and 100% of Class A non-voting Common Stock. On October 19, 1998, ICH repurchased from IMH 937,084 shares of ICH Common Stock and 456,916 shares of ICH Class A Common Stock, which represented all ICH Common Stock that IMH owned, and eliminating any recognition of earnings or losses from ICH. For more information on the results of operations of ICH, refer to Impac Commercial Holdings, Inc.'s Annual Report on Form 10-K filed with the Securities and Exchange Commission on February 26, 1999.

Non-Interest Expense

General and Administrative and Other Expense

General and administrative and other expense increased to $2.3 million during 1998 as compared to $836,000 during 1997. The increase in general and administrative and other expense was primarily related to property expense on a commercial office building in which the Company had a 50% ownership interest, which was sold to ICH in October 1998. Property expense increased to $623,000 during 1998 as compared to $109,000 during 1997.

Professional Services

Professional services increased to $2.2 million during 1998 as compared to $1.1 million during 1997. Professional services primarily includes intercompany allocations of MIS, accounting and executive management services from IFC which increased to $968,000 during 1998 as compared to $385,000 during 1997. Professional services also includes outside legal, accounting and tax work performed for the Company.

Advisory Fees

Earnings were positively affected by a reduction in advisory fees resulting from the Company's buyout of its management agreement with ICAI in December 1997. As a result of the buyout, there were no advisory fees paid by IMH during 1998 as compared to $6.2 million in advisory fees paid by IMH during 1997.

Provision for Loan Losses

The Company recorded loan loss provisions of $4.4 million during 1998 as compared to $6.8 million during 1997. The amount provided for loan losses during 1998 decreased primarily due to a reduction in exposure to future losses through the sale of delinquent loans and the transfer of certain loans from the held-for-investment to the held-for-sale portfolio (as explained below).

Credit Exposures

Non-performing Assets. The outstanding unpaid principal balance of non-performing assets totaled $80.7 million at December 31, 1998 as compared to $50.1 million at December 31, 1997. The increase in non-performing assets was primarily due to delinquent mortgage loans with high loan-to-value ratios, which were purchased in 1997, and the seasoning of mortgage loans held for long-term investment. Of the total non-performing assets at December 31, 1998 and 1997, other real estate owned represented $9.2 million and $5.7 million, respectively, in unpaid principal balance. The carrying amount of other real estate owned, after writing down the mortgage loan to the broker's price opinion or appraised value, was $8.5 million and $5.7 million at December 31, 1998 and 1997, respectively. The Company recorded losses on the disposition of other real estate owned of $1.7 million during 1998 as compared to gains on disposition of other real estate owned of $433,000 during 1997.

The following table summarizes the unpaid principal balance of the Company's non-performing assets included in its mortgage loan portfolios for the periods shown (in thousands):

	At December 31,	
	1998	1997
Mortgage Loans Held-for-Sale:		
Non-accrual	$ 15,328	$ 5,740
Other real estate owned	—	—
Total mortgage loans held-for-sale	15,328	5,740
Mortgage Loans Held-for-Investment:		
Non-accrual	6,870	7,627
Other real estate owned	1,437	1,415
Total mortgage loans held-for-investment	8,307	9,042
CMO collateral:		
Non-accrual	49,305	31,056
Other real estate owned	7,739	4,247
Total CMO collateral	57,044	35,303
Total mortgage loan portfolios	$ 80,679	$ 50,085

Delinquencies. At December 31, 1998, loans that were delinquent 30 days or more, as a percentage of the outstanding servicing balance of the mortgage loan portfolios, was 10.98% as compared to 9.81% at December 31, 1997. The following table summarizes the unpaid principal balance of the Company's delinquent mortgage loans included in its mortgage loan portfolios for the periods shown (in thousands):

	At December 31,	
	1998	1997
Mortgage Loans Held-for-Sale:		
30-59 days delinquent	$ 6,976	$ 21,309
60-89 days delinquent	1,448	3,395
90 or more days delinquent (1)	15,328	5,740
Total mortgage loans held-for-sale	23,752	30,444
Mortgage Loans Held-for-Investment:		
30-59 days delinquent	2,384	2,999
60-89 days delinquent	271	3,375
90 or more days delinquent (1)	6,870	7,627
Total mortgage loans held-for-investment	9,525	14,001
CMO collateral:		
30-59 days delinquent	63,953	59,223
60-89 days delinquent	18,695	16,034
90 or more days delinquent (1)	49,305	31,056
Total CMO collateral	131,953	106,313
Total mortgage loan portfolios	$ 165,230	$ 150,758

(1) Includes loans in foreclosure and delinquent bankruptcies.

Provision for Loan Losses. The Company's total allowance for loan losses expressed as a percentage of Gross Loan Receivables which includes loans held-for-investment, CMO collateral and finance receivables, increased to 0.47% at December 31, 1998 as compared to 0.32% at December 31, 1997. The Company recorded net loan loss provisions of $4.4 million during 1998 as compared to $6.8 million during 1997. The amount provided for loan losses during 1998 decreased primarily due to a reduction in exposure to future losses through the sale of delinquent loans and the transfer of certain loans from the held-for-investment to the held-for-sale portfolio, which resulted in a mark-to-market adjustment. The allowance for loan losses is determined primarily on the basis of management's judgment of net loss potential including specific allowances for known impaired loans, changes in the nature and volume of the portfolio, value of the collateral and current economic conditions that may affect the borrowers' ability to pay.

RESULTS OF OPERATIONS— IMPAC FUNDING CORPORATION

Year Ended December 31, 1999 as compared to Year Ended December 31, 1998

Net Earnings (Loss)

IFC recorded net earnings of $4.3 million during 1999 as compared to a net loss of $(14.0) million during 1998. Earnings increased during 1999 as compared to 1998 primarily as the mortgage market stabilized and recovered from the liquidity crisis, which occurred during the latter part of 1998. As the mortgage market recovered during 1999, IFC returned to overall profitability, which in large part was due to the profitability on the sale of its mortgage loans. During 1998, IFC sold loans at significant losses to meet margin calls and raise liquidity. In addition, IFC recorded non-cash write-down on MSRs and investment securities available-for-sale.

Net Interest Income

Net interest income decreased to $272,000 during 1999 as compared to $7.8 million during 1998 as average mortgage loans held-for-sale decreased 50% to $240.1 million as compared to $476.1 million, respectively. Average mortgage loans held-for-sale decreased due to the shorter accumulation and holding period of mortgage loans held-for-sale and a decrease in mortgage loan acquisitions. During 1999, IFC primarily sold loans monthly on a whole loan basis as opposed to quarterly securitizations, which occurred during 1998. Monthly whole loan sales were completed during 1999 in order to reduce interest rate and market risk exposures and to maintain strong liquidity levels. In addition, mortgage loan acquisitions decreased 23% to $1.7 billion during 1999 as compared to mortgage loan acquisitions of $2.2 billion during 1998. Mortgage loan acquisitions decreased during 1999 as compared to 1998 due to the residual effects of the deterioration of the mortgage-backed securitization market, which occurred during the latter part of 1998. In response to the liquidity crisis, IFC raised interest rates on its loan programs and decreased the amount of premiums paid on its loan acquisitions, which caused some of IFC's correspondent sellers to use other sources for the funding of their mortgage loans. During 1999, IFC continued to rebuild its mortgage loan acquisitions to previous levels by offering its sellers competitive and flexible mortgage products. As such, mortgage loan acquisitions increased 48% to $548.2 million during the fourth quarter of 1999 as compared to $370.5 million during the fourth quarter of 1998.

Non-Interest Income

Non-interest income increased to $33.3 million during 1999 as compared to $(5.7) million during 1998 as gain on sale of loans increased to $27.1 million during 1999 as compared to $(11.7) million during 1998. In line with the Company's overall strategy to reduce interest rate and market risk exposure and to maintain strong liquidity levels, IFC sold mortgage loans on a whole loan basis for cash during 1999, as opposed to sales through asset-backed securitizations for non-cash gains, which occurred during 1998. During 1999, IFC sold mortgages totaling $824.1 million, on a servicing released basis, to third party investors as compared to loan sales of $856.2 million during 1998. The sale of loans on a servicing released basis during 1999 reduced IFC's exposure to further prepayment risk. IFC also securitized $360.1 million in REMICs during 1999 as compared to $907.5 million in REMICs during 1998. The increase in gain on sale of loans was partially offset by a decrease in loan servicing income during 1999 as compared to 1998. Loan servicing income decreased to $5.2 million during 1999 as compared to $7.1 million during 1998 as IFC sold MSRs and completed loan sales

on a servicing released basis. Total unpaid principal balance of mortgage loans at the time MSRs were sold was $2.3 billion.

Non-Interest Expense

Non-interest expense increased 5% to $26.0 million during 1999 as compared to $24.8 million during 1998. Non-interest expense during 1999 was positively affected by decreases in personnel expense and impairment and amortization of MSRs. Personnel expense decreased 18% to $7.3 million as compared to $8.9 million during 1998. Personnel expense decreased primarily due to a reduction in staff which occurred during the fourth quarter of 1998 and carried into 1999. During the fourth quarter of 1998, IFC reduced staff in anticipation of decreased loan acquisitions due to the deterioration of the mortgage-backed securitization market. The reduction in staff also contributed to increased liquidity from operating activities. Impairment of MSRs decreased to $1.1 million during 1999 as compared to $3.7 million during 1998 as the mortgage market recovered during 1999. Impairment of MSRs recorded in 1998 was primarily due to the deterioration of the mortgage-backed securitization market. Amortization of MSRs decreased to $5.3 million as compared to $6.4 million as IFC sold MSRs and completed whole loan sales on a servicing released basis.

The decreases in personnel expense and impairment and amortization of MSRs were offset by increases in write-down on securities available-for-sale and general and administrative and other expense. Write-down on securities available-for-sale increased to $4.3 million during 1999 as compared to zero during 1998. The write-down on securities available-for-sale was due to the complete write-off of an investment security deemed to have no value. The increase in general and administrative and other expense during 1999 was primarily due to costs associated with the operation of the wholesale and retail origination division, which began operations in 1999, and costs associated with the application of the Bank charter.

Year Ended December 31, 1998 as compared to Year Ended December 31, 1997

Net Earnings (Loss)

IFC recorded a net loss of $(14.0) million for the year ended December 31, 1998 as compared to net earnings of $8.4 million for the same period in 1997. Earnings decreased for the year ended December 31, 1998 as compared to the same period in 1997 primarily as a result of net losses on sale of mortgage loans and non-cash charges for the write-down of MSRs and investment securities available-for-sale. The net loss on sale of mortgage loans and non-cash charges was due to the deterioration of the mortgage-backed securitization market, as previously discussed. In addition, earnings for the year ended December 31, 1998 were negatively affected by increases in personnel expense, amortization of MSRs and general and administrative and other expense.

Net Interest Income

Net interest income increased 22% to $7.8 million during 1998 as compared to $6.4 million during 1997. Although mortgage loan acquisitions decreased 15% to $2.2 billion during 1998 as compared to $2.6 billion during 1997, IFC had higher average mortgage loan balances outstanding as the mortgage-backed securitization and whole loan sales market deteriorated during the latter half of 1998 and made it more difficult for IFC to securitize or sell mortgage loans. Average mortgage loans held-for-sale increased 5% to $476.1 million during 1998 as compared to $455.3 million during 1997. The weighted average yield on mortgage loans held-for-sale increased to 9.47% during 1998 as compared to 9.31% during 1997.

In addition, IFC's total net interest spread increased to 1.29% during 1998 as compared to 1.10% during 1997. The increase in total net interest spread was primarily due to a reduction of borrowings on residual interests in securities, which occurred in December of 1997. These borrowings were paid off as part of the Company's termination of its management agreement with ICAI. Total interest expense on these borrowings was $3.7 million during 1997 with a yield of 11.81%.

Non-Interest Income

Non-interest income decreased to $(5.7) million during 1998 as compared to $24.2 million during 1997. Non-interest income decreased primarily due to a reduction of $31.1 million in gain on sale of loans, a mark-to-market loss of $805,000 on investment securities available-for-sale, and a decrease of $1.3 million on gain on sale of investment securities.

During 1998, IFC securitized $907.5 million of mortgages and sold whole loans to third party investors totaling $856.2 million, resulting in net loss on sale of loans of $11.7 million, during 1998. This compares to securitizations of $878.0 million and whole loan sales to third parties of $501.7 million, resulting in net gain on sale of loans of $19.4 million, during 1997. The increase in loan sales to third parties during 1998 as compared to 1997 was the result of IFC selling mortgage loans to reduce its outstanding borrowings on its reverse repurchase facilities in order to meet margin calls from its lenders. The loss on loans sold during 1998 as compared to gain on loans sold during 1997 was the result of lower prices IFC received on its loans. The Company felt it was important to protect shareholder value and increase liquidity by selling out of its mortgage loan positions at losses rather than take additional interest rate and market risk by retaining the loans for securitization.

Loan servicing income increased 73% to $7.1 million for 1998 as compared to $4.1 million for 1997 due to the continued increase in IFC's servicing portfolio. IFC continues to build its loan servicing portfolio as IFC generally retains loan servicing rights on mortgage loans acquired. Total loans serviced at December 31, 1998 were 33,414, or $3.7 billion in principal balance of mortgages, as compared to 28,494, or $3.0 billion in principal balance of mortgages, at December 31, 1997.

Non-Interest Expense

Non-interest expense increased to $24.8 million during 1998 as compared to $16.0 million during 1997. The increase in expense was primarily the result of increases in personnel expense of $2.1 million, amortization of MSRs of $3.5 million and a non-cash impairment charge on MSRs of $3.7 million.

Personnel expense increased 31% to $8.9 million during 1998 as compared to $6.8 million during 1997 primarily due to an increase in staff and incentive compensation during the first nine months of 1998 as IFC's production volumes increased. However, in October of 1998 IFC reduced staff by approximately 25% as production volumes decreased during the fourth quarter of 1998 due to interest rate and purchase price adjustments IFC made on its loan programs.

Amortization of MSRs increased to $6.4 million during 1998 as compared to $2.8 million during 1997 due to continued growth of IFC's servicing portfolio. Since December 31, 1997, the Company has securitized $907.5 million in principal balance of mortgage loans and, accordingly, has capitalized MSRs related to those securitizations which are amortized in proportion to, and over the period of expected net servicing income. In addition, during 1998 IFC recorded an impairment charge of $3.7 million on its MSRs as a result of a decrease in their value.

Liquidity and Capital Resources

Overview

Historically, the Company's business operations are primarily funded from monthly interest and principal payments from its mortgage loan and investment securities portfolios, adjustable- and fixed-rate CMO financing, reverse repurchase agreements secured by mortgage loans, borrowings secured by mortgage-backed securities, proceeds from the sale of mortgage loans and the issuance of REMICs and proceeds from the issuance of Common Stock through secondary stock offerings, DRSPP, and its structured equity shelf program ("SES Program"). The acquisition of mortgage loans and mortgage-backed securities by the Long-Term Investment Operations are primarily funded from monthly principal and interest payments, reverse repurchase agreements, CMO financing, and proceeds from the sale of Common Stock. The acquisition of mortgage loans by the Conduit Operations are funded from reverse repurchase agreements, the sale of mortgage loans and mortgage-backed securities and the issuance of REMICs. Short-term warehouse financing, finance receivables, provided by the Warehouse Lending Operations are primarily funded from reverse repurchase agreements. During 1999, the Company issued no new shares of Common Stock through stock offerings or through its SES Program and issued only minimal shares of Common Stock through its DRSPP. In addition, during 1999 the Company suspended the issuance of any new shares of Common Stock under the DRSPP.

The Company's ability to meet its long-term liquidity requirements is subject to the renewal of its credit and repurchase facilities and/or obtaining other sources of financing, including additional debt or equity from time to time. Any decision by the Company's lenders and/or investors to make additional funds available to the Company in the future will depend upon a number of factors, such as the Company's compliance with the terms of its existing credit arrangements, the Company's financial performance, industry and market trends in the Company's various businesses, the general availability of and rates applicable to financing and investments, such lenders' and/or investors' own resources and policies concerning loans and investments, and the relative attractiveness of alternative investment or lending opportunities.

Results of Liquidity during 1999

The deterioration of the mortgage-backed securitization market during the latter half of 1998 created a lack of liquidity for the Company as the Company's lenders made margin calls on their reverse repurchase agreements. Margin calls result from the Company's lenders evaluating the market value of underlying collateral securing the reverse repurchase agreements and requiring additional equity or collateral on the reverse repurchase agreements. These margin calls resulted in the Company delaying its third quarter dividend, which was paid on January 6, 1999, and selling mortgage loans and mortgage-backed securities, during the fourth quarter of 1998, at significant losses. During the fourth quarter of 1998, the Company completed the sale of $250.4 million of mortgage loans and $8.9 million of mortgage-backed securities, which increased the Company's liquidity by $13.6 million, at the time of sale, after paying down related reverse repurchase agreements. By selling mortgage loans and paying down outstanding borrowings on reverse repurchase facilities, the Company reduced its exposure to future margin calls.

However, the market disruptions during 1998 caused several public companies to file for protection from their creditors under the U.S. Bankruptcy Code. This had the effect of causing reduced investor confidence with certain sectors of the financial services industry, particularly REITs, which in turn caused stock prices to fall sharply. As a result of this decline in stock prices, the Company suspended any purchases of its Common Stock through its DRSPP and was unable to access the capital markets and raise additional cash. In response to these market conditions and availability of capital, the Company increased the pricing of its loans and limited the amount of premiums paid in acquiring mortgage loans. In anticipation of reduced production from increased loan rates and decreased loan pricing, the Company reduced staffing levels, thereby increasing liquidity from operating activities.

As the mortgage market stabilized during 1999, the Company restructured its balance sheet and generated cash internally to meet its funding needs. IFC completed monthly whole loan sales on a servicing released basis, which provided liquidity throughout 1999 to acquire mortgage loans and fund operations. The Company also completed a re-securitization of a portion of its investment securities available-for-sale in October 1999, which raised additional cash of approximately $23.4 million after repaying short-term borrowings secured by the investment securities. The cash proceeds were used to acquire mortgages from IFC, increase outstanding lending by the Warehouse Lending Operations, repurchase Common Stock and other business expansion. The Company successfully repurchased 2.0 million shares of Common Stock for $9.9 million with the cash generated by the re-securitization and reduced its reliance on reverse repurchase agreements. Reverse repurchase agreements to finance its investment securities decreased to zero at December 31, 1999 as compared to $24.1 million at December 31, 1998. The Company continued to maintain reduced leverage and strong liquidity levels during 1999. The Company's debt-to-equity ratio increased slightly to 6.0:1 at December 31, 1999 as compared to 5.6:1 at December 31, 1998, which was well within the Company's target range. This compares to a debt-to-equity ratio of 7.9:1 at September 30, 1998, which was prior to the deterioration of the mortgage-backed securitization market during the fourth quarter of 1998. During 1999, the Company experienced no margin calls on its reverse repurchase facilities.

The Company believes that current liquidity levels, available financing facilities and additional liquidity provided by operating activities, as projected for 2000, will adequately provide for the Company's projected funding needs, asset growth and the payment of dividends. As such, the Board of Directors has announced a dividend policy for 2000 that allows the Company to expand its business operations and focus on rebuilding the Company's balance sheet without the diluted effect of offering additional shares of Common Stock at current market levels. During 2000, the Company plans to distribute 100% of taxable earnings. However, any future margin calls and, depending upon the state of the mortgage industry, terms of any sale of Mortgage Assets may adversely affect the Company's ability to pay dividends in future periods or subject the Company to future losses.

Definitive Agreement to Acquire Thrift and Loan Charter. During the first quarter of 1999, the Company completed a definitive agreement to acquire a Bank. As provided for in the agreement, the Company submitted its application in the second quarter of 1999 for a change of control to the state and federal regulatory agencies for their approval. During the process of reviewing the application, the federal agency raised certain issues. The Company was not able to give the federal agency sufficient comfort with respect to those issues without modifying its proposal. The Company submitted a new application to state and federal regulatory agencies in the first quarter of 2000. The new application was modified from the previous application in several key areas and to more clearly define the Bank as a stand-alone operation that is not reliant upon the Company for its success. It is anticipated that the Bank will market its own unique loan products, which will include mortgages, consumer equity loans and loans on small commercial and multi-family properties. However, there are no assurances that the new application for change of control will be received favorably by either of the state or federal regulatory agencies. In the event that the Company is unsuccessful in its efforts to obtain the Bank charter, management believes that it will have no adverse impact on the future profitability of the Company.

Sources of Liquidity

Long-Term Investment Operations: The Long-Term Investment Operations uses CMO borrowings to finance substantially all of its mortgage loan portfolio. Terms of the CMO borrowings require that an independent third party custodian hold the mortgages. The maturity of each class is directly affected by the rate of principal prepayments on the related collateral. Equity in the CMOs is established at the time the CMOs are issued at levels sufficient to achieve desired credit ratings on the securities from rating agencies. The amount of equity invested in CMOs by the Long-Term Investment Operations is also determined by the Company based upon the anticipated return on equity as compared to the estimated proceeds from additional debt issuance. Total credit loss exposure is limited to the equity invested in the CMOs at any point in time. At December 31, 1999, the Long-Term Investment Operations had $850.8 million of CMO borrowings used to finance $949.7 million of CMO collateral.

Prior to October 1999, the Long-Term Investment Operations pledged mortgage-backed securities as collateral to borrow funds under reverse repurchase agreements. The terms under these reverse repurchase agreements were generally for 30 days with interest rates ranging from one-month LIBOR plus 0.45% to 2.00% depending on the type of collateral provided. However, during October 1999, the Company re-securitized a portion of its mortgage-backed securities portfolio with notes. As of December 31, 1999, the Long-Term Investment Operations had $31.3 million outstanding under these notes, which were secured by $49.6 million in fair market value of mortgage-backed securities. The Company still has the ability to borrow funds under the reverse repurchase agreements.

During 1999, the Company raised capital of $1.0 million from the sale of 216,156 shares of Common Stock issued through its DRSPP.

Conduit Operations: The Conduit Operations has entered into warehouse line agreements to obtain financing of up to $600.0 million from the Warehouse Lending Operations to provide IFC mortgage loan financing during the period that IFC accumulates mortgage loans until the mortgage loans are securitized or sold. The margins on IFC's reverse repurchase agreements are based on the type of collateral provided and generally range from 95% to 98% of the fair market value of the collateral. The interest rates on the borrowings are indexed to prime, which was 8.50% at December 31, 1999. As of December 31, 1999, the Conduit Operations had $66.1 million outstanding under the warehouse line agreements. IFC also has an uncommitted warehouse line agreement to obtain financing from a major investment bank. As of December 31, 1999 and 1998, there was $181,000 and $25.0 million outstanding under the warehouse line.

During 1999, the Conduit Operations securitized $360.1 million of mortgage loans as REMICs and sold $824.1 million, in unpaid principal balance, of mortgage loans to third party investors. In addition, IFC sold $638.3 million, in unpaid principal balance, of mortgage loans to the Long-Term Investment Operations during 1999.

Warehouse Lending Operations: The Warehouse Lending Operations finances the acquisition of mortgage loans by the Long-Term Investment Operations and Conduit Operations primarily through borrowings on reverse repurchase agreements with third party lenders. IWLG has an uncommitted repurchase facility with a major investment bank to finance the Warehouse Lending Operations as needed. Terms of the reverse repurchase agreement requires that the mortgages be held by an independent third party custodian giving the Warehouse Lending Operations the ability to

borrow against the collateral as a percentage of the outstanding principal balance. The borrowing rates vary from 85 basis points to 200 basis points over one-month LIBOR, depending on the type of collateral provided. The margins on the reverse repurchase agreement is based on the type of mortgage collateral provided and generally range from 70% to 98% of the fair market value of the collateral. At December 31, 1999, the Warehouse Lending Operations had $539.7 million outstanding on the reverse repurchase facility.

Cash Flows

Operating Activities - During 1999, net cash provided by operating activities was $55.8 million. Cash provided by operating activities was primarily from net earnings of $22.3 million.

Investing Activities - During 1999, net cash used in investing activities was $64.1 million. Cash used in investing activities was primarily due to the acquisition of mortgage loans from IFC. Cash used to acquire mortgage loans was partially offset by cash provided from repayment of CMO collateral and finance receivables.

Financing Activities - During 1999, net cash used in financing activities was $5.5 million. Cash used in financing activities was primarily due to repayments of CMOs, payment of cash dividends and repurchase of Common Stock. Cash used in financing activities was offset by cash provided from increased borrowings on reverse repurchase agreements and from the issuance of new CMOs.

Inflation

The Consolidated Financial Statements and Notes have been prepared in accordance with GAAP, which require the measurement of financial position and operating results in terms of historical dollars without considering the changes in the relative purchasing power of money over time due to inflation. The impact of inflation is reflected in the increased costs of the Company's operations. Unlike industrial companies, nearly all of the assets and liabilities of the Company's operations are monetary in nature. As a result, interest rates have a greater impact on the Company's operations' performance than do the effects of general levels of inflation. Inflation affects the Company's operations primarily through its effect on interest rates, since interest rates normally increase during periods of high inflation and decrease during periods of low inflation. During periods of increasing interest rates, demand for mortgage loans and a borrower's ability to qualify for mortgage financing in a purchase transaction may be adversely affected. During periods of decreasing interest rates, borrowers may prepay their mortgages, which in turn may adversely affect the Company's yield and subsequently the value of its portfolio of Mortgage Assets.

Year 2000 Compliance

After completing all phases of its Year 2000 Project Plan, the Company experienced no problems as a result of Year 2000 issues. Both in-house information technology systems and non-information technology systems functioned according to the Company's internal Year 2000 Project Plan. In addition, the Company's vendors, who provide the Company with both integrated and non-integrated systems data, functioned without any Year 2000 related problems as well. Even though the Company does not expect any "residual" Year 2000 issues to affect the Company's operations, there can be no assurance that the Company will not be affected in the future. The Company paid a total of $273,000 to an outside vendor for Year 2000 project work during the year ended December 31, 1999.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

General

A significant portion of the Company's revenues and earnings are derived from net interest income and, accordingly, the Company strives to manage its interest-earning assets and interest-bearing liabilities to generate what management believes to be an appropriate contribution from net interest income. When interest rates fluctuate, the Company can be adversely affected by changes in the fair market value of its assets and liabilities and by the interest spread the Company earns on interest-earning assets and interest-bearing liabilities. The Company derives income from the differential spread between interest earned on interest-earning assets and interest paid on interest-bearing liabilities.

Any change in interest rates affect both income received and income paid from these assets in varying and typically in unequal amounts and may compress the Company's interest rate spread and adversely affect overall earnings.

Therefore, the Company seeks to control the volatility of the Company's performance due to changes in interest rates through asset/liability management. The Company attempts to achieve an appropriate relationship between interest rate sensitive assets and interest rate sensitive liabilities. Although the Company manages other risks, such as credit, operational and liquidity risk in the normal course of business, management considers interest rate risk to be a significant market risk which could potentially have the largest material effect on the Company's financial condition and results of operations. As the Company has only invested or borrowed in U.S. dollar denominated financial instruments, the Company is not subject to foreign currency exchange risk.

As part of its asset/liability management process, the Company performs various interest rate simulations that calculate the affect of potential changes in interest rates on its interest-earning assets and interest-bearing liabilities and their affect on overall earnings. This analysis assumes instantaneous parallel shifts in the yield curve and to what degree those shifts affect net interest income. In addition, various modeling techniques are used to value interest sensitive mortgage-backed securities, including interest-only securities. The value of mortgage-backed securities is determined using a discounted cash flow model using prepayment rate, discount rate and credit loss assumptions.

Interest Rate Sensitive Assets and Liabilities

Interest rate risk management is the responsibility of the Company's Asset and Liability Committee ("ALCO"), which reports to the Company's Board of Director's on a monthly basis. ALCO establishes policies that monitor and coordinate the Company's sources, uses and pricing of its funds. ALCO also attempts to reduce the volatility in net interest income by managing the relationship of interest rate sensitive assets to interest rate sensitive liabilities.

The matching of assets and liabilities may be analyzed by examining the extent to which such assets and liabilities are "interest rate sensitive" and by monitoring an institution's interest rate sensitivity "gap." An asset or liability is said to be interest rate sensitive within a specific time period if it will mature or reprice within that time period. The interest rate sensitivity gap is defined as the difference between the amount of interest-earning assets maturing or repricing within a specific time period and the amount of interest-bearing liabilities maturing or repricing within that time period. A gap is considered positive when the amount of interest rate sensitive assets exceeds that amount of interest rate sensitive liabilities. A gap is considered negative when the amount of interest rate sensitive liabilities exceeds the amount of interest rate sensitive assets. During a period of falling interest rates, the net earnings of an institution with a positive gap, theoretically, may be adversely affected due to its interest-earning assets repricing to a greater extent than its interest-bearing liabilities. Conversely, during a period of rising interest rates, theoretically, the net earnings of an institution with a positive gap position may increase as it is able to invest in higher yielding interest-earning assets at a more rapid rate than its interest-bearing liabilities reprice. However, the gap analysis does not take into consideration constraints on the repricing of interest rates of ARM assets in a given period resulting from periodic and lifetime cap features, the behavior of various indexes applicable to the Company's assets and liabilities or the affects of off-balance sheet financial instruments, particularly interest rate caps, on net interest income, see "—Changes in Interest Rates."

The Company manages its interest rate risk by (1) retaining adjustable-rate mortgages to be held for long-term investment, (2) selling fixed-rate mortgages on a whole-loan basis, (3) securitizing both adjustable- and fixed-rate mortgages through the issuance of CMOs, and (4) the purchase of LIBOR interest rate caps, see "—Hedging." The Company retains adjustable-rate mortgages, which are generally indexed to six-month LIBOR and reprice every six months, to be held for investment or as CMO collateral. The Company also securitizes both variable- and fixed-rate mortgages as CMOs to reduce its interest rate risk as CMOs provide a net interest spread between the interest income on the mortgages and the interest and other expenses associated with the CMO financing. In addition, the Company purchases LIBOR interest rate caps to provide some protection against any resulting basis risk shortfall on the related liabilities. The interest rate caps purchased are based upon the principal balance that would result under an assumed prepayment speed.

The Company does not currently maintain a securities trading portfolio. As a result, the Company is not exposed to market risk as it relates to trading activities. The Company's investment securities portfolio is available-for-sale, which requires the Company to perform market valuations of the portfolio in order to properly record the portfolio at the lower

of cost or market. Therefore, the Company continually monitors the interest rates of its investment securities portfolio as compared to prevalent interest rates in the market.

The following table summarizes the amount of interest-earning assets and interest-bearing liabilities outstanding at December 31, 1999 (dollar amounts in thousands), which are anticipated by the Company to reprice or mature in each of the future time periods shown. The amount of assets and liabilities shown which reprice or mature during a particular period were determined in accordance with the earlier of term to repricing or the contractual term of the asset or liability as adjusted for scheduled and unscheduled repayments. Unscheduled prepayment rates are assumed on substantially all of the Company's mortgage-backed security and loan portfolios and are based on historic loan prepayment experience and anticipated future prepayments. The table does not include assets and liabilities that are not interest rate sensitive such as interest receivables and payables, prepaid expenses and accrued expenses.

	2000	2001	2002	2003	2004	Over 5 Years (4)	Total	Fair Value
Interest sensitive assets:								
Cash equivalents	$ 20,152	$ —	$ —	$ —	$ —	$ —	$ 20,152	$ 20,152
Average interest rate	4.28 %	— %	— %	— %	— %	— %	4.28 %	
Investment securities (1)	11,942	8,384	9,514	10,487	10,786	42,093	93,206	93,206
Average interest rate	13.79 %	13.79 %	13.79 %	13.79 %	13.79 %	13.79 %	13.79 %	
Finance receivables	197,119	—	—	—	—	—	197,119	197,119
Average interest rate	8.97 %	— %	— %	— %	— %	— %	8.97 %	
CMO collateral (2)	409,262	108,720	56,424	48,092	41,164	286,015	949,677	938,784
Average interest rate	8.11 %	8.38 %	8.51 %	8.54 %	8.58 %	7.54 %	8.03 %	
Loans held-for-investment (3)	32,212	47,941	24,235	30,585	20,551	207,911	363,435	366,066
Average interest rate	7.89 %	8.30 %	8.76 %	8.75 %	8.75 %	7.16 %	7.70 %	
Due from affiliates	14,500	—	—	—	—	—	14,500	14,500
Average interest rate	8.33 %	— %	— %	— %	— %	— %	8.33 %	
Total interest-sensitive assets	$ 685,187	$ 165,045	$ 90,173	$ 89,164	$ 72,501	$ 536,019	$ 1,638,089	$ 1,629,827
Average interest rate	8.34 %	8.63 %	9.14 %	9.23 %	9.40 %	7.88 %	8.36 %	
Interest sensitive liabilities:								
CMO borrowings	$ 591,144	$ 36,296	$ 31,276	$ 26,944	$ 23,207	$ 140,453	$ 849,320	$ 844,852
Average interest rate	7.15 %	7.15 %	7.15 %	7.15 %	7.15 %	7.15 %	7.15 %	
Reverse repurchase agreements	539,687	—	—	—	—	—	539,687	539,687
Average interest rate	6.41 %	— %	— %	— %	— %	— %	6.41 %	
Borrowings secured by Securities available-for-sale	9,178	6,505	4,607	3,261	2,306	5,476	31,333	34,393
Average interest rate	13.00 %	13.00 %	13.00 %	13.00 %	13.00 %	13.00 %	13.00 %	
Senior subordinated debt	—	—	—	—	6,691	—	6,691	6,198
Average interest rate	— %	— %	— %	— %	11.00 %	— %	11.00 %	
Due to affiliates	2,945	—	—	—	—	—	2,945	2,945
Average interest rate	8.00 %	— %	— %	— %	— %	— %	8.00 %	
Total interest-sensitive liabilities	$ 1,142,954	$ 42,801	$ 35,883	$ 30,205	$ 32,204	$ 145,929	$ 1,429,976	$ 1,428,075
Average interest rate	6.85 %	8.04 %	7.90 %	7.78 %	8.37 %	7.37 %	7.02 %	
Interest rate sensitivity gap (5)	$ (457,767)	$ 122,244	$ 54,290	$ 58,959	$ 40,297	$ 390,090	$ 208,113	
Cumulative interest rate Sensitivity gap	$ (457,767)	$ (335,523)	$ (281,233)	$ (222,274)	$ (181,977)	$ 208,113		
Cumulative gap ratio %	(27.95) %	(20.48) %	(17.17) %	(13.57) %	(11.11) %	12.70 %		

(1) The over 5 year category includes "interest-only" securities of $30.8 million.
(2) Includes unamortized net premiums and unamortized securitization costs of $28.8 million and $11.9 million, respectively.
(3) Includes unamortized net premiums of $2.0 million.
(4) CMO collateral and loans held-for-investment include non-accrual loans of $42.8 million and $8.3 million, respectively.
(5) Interest rate sensitivity gap represents the difference between interest-earning assets and interest-bearing liabilities.

As the Company's estimated interest rate sensitivity gap is negative during 2000, net interest income could be negatively affected by an increase in interest rates as more interest-bearing liabilities could reprice upwards during 2000 than interest-bearing assets. Conversely, a decrease in interest rates could have a positive affect on net interest income during 2000 as more interest-bearing liabilities could reprice downwards during 2000 than interest-bearing assets. The estimated cumulative negative gap during 2000 of $457.8 million compares to an estimated cumulative positive gap for 1999 of $303.6 million. The shift from an estimated cumulative positive gap in 1999 to an estimated cumulative negative gap in 2000 is primarily the result of the Company retaining $321.6 million of mortgage loans, during the fourth quarter of 1999, that have fixed interest rates for initial two-, three-, and five-year periods, which subsequently change to adjustable interest rates thereafter. Since these estimates are based upon numerous assumptions, such as the expected maturities of the Company's interest-earning assets and interest-bearing liabilities, the Company's actual sensitivity to interest rate changes could vary significantly if actual experience differs from those assumptions used in making the calculations. In addition, the estimated impacts of parallel shifts in interest rates and the resulting effect on net interest income does consider increases or decreases in premium amortization and securitization expenses due to possible increases or decreases in loan prepayments, which could also vary if actual experience differs from the prepayment assumptions used.

Changes in Interest Rates

Although the static gap methodology is widely accepted in identifying interest rate risk, it does not take into consideration changes that may occur in investment and financing strategies, changes in the yield curve, changes in hedging strategy, changes in prepayment speeds and changes in business volumes. Therefore, in addition to measuring interest rate risk via a gap analysis, the Company measures the sensitivity of its net interest income to changes in interest rates affecting interest sensitive assets and liabilities using simulations. The simulations consider the affect of interest rate changes on interest sensitive assets and liabilities as well as interest rate caps (off-balance sheet items). Changes in interest rates are defined as instantaneous and sustained movements in interest rates in 100 basis point increments. The Company estimates its net interest income for the next twelve months assuming no changes in interest rates from those at period end. Once the base case has been estimated, calculations are made for each of the defined changes in interest rates, to include any associated differences in the anticipated prepayment speed of loans. Those results are then compared against the base case to determine the estimated change to net interest income.

The following table (dollar amounts in millions) estimates the financial impact to net interest income from various instantaneous and parallel shifts in interest rates based on the Company's on- and off-balance sheet structure as of December 31, 1999 and 1998. Since, these estimates are based upon numerous assumptions, such as expected prepayment rates and the shape of the yield curve, the Company's actual sensitivity to interest rate changes could differ significantly as compared to actual results.

	2000		**1999**	
Changes in Interest Rates (In Basis Points)	**Change in Net Interest Income (1)**		**Change in Net Interest Income (1)**	
	($)	**(%)**	**($)**	**(%)**
+200	(9.2)	(25)	(1.9)	(6)
+100	(4.2)	(12)	(4.4)	(14)
-100	2.6	7	2.1	7
-200	1.0	3	4.9	16

(1) The dollar and percentage changes represent net interest income, for the next twelve months, in a stable interest rate environment versus the change in net interest income in the various instantaneous, parallel rate change simulations.

The estimated decreases in net interest income in an increasing rate environment during 2000 as compared to 1999 is primarily due to (1) an estimated negative gap during year 2000 of $457.8 million, as shown in the static gap table above, and (2) the lag in the repricing of the indices to which the Company's adjustable rate loans and mortgage-backed securities are tied as compared to the borrowings that fund these assets. As interest rates increase, an estimated $1.1 billion of the Company's interest rate sensitive liabilities contractually mature or reprice during 2000 as compared to $685.2 million of interest rate sensitive assets that are estimated to contractually mature or reprice during 2000. As of December 31, 1999, mortgage loans held-for-investment, of which approximately $350.0 million were retained during the fourth quarter of 1999, were financed by reverse repurchase agreements, which are subject to daily repricing based on one-month LIBOR plus a spread. Therefore, as of December 31, 1999, loans held-for-investment with primarily two- to five-year repricing dates were matched against (financed with) liabilities with daily repricing characteristics. However, during January 2000, these loans were used as collateral for CMOs that have lower financing costs than reverse repurchase agreements but were not reflected in the gap analysis or the calculations of changes in net interest income as the CMO was completed subsequent to year-end. Additionally, because the Company's adjustable rate CMO collateral is tied to various indices, primarily six-month LIBOR, and the corresponding CMO financing is primarily tied to one-month LIBOR, the Company's interest rate sensitive liabilities reprice faster than its interest rate sensitive assets, which could create negative results in net interest income over the near term (12-month horizon) during periods of increasing interest rates.

The following table presents the extent to which changes in interest rates and changes in the volume of interest rate sensitive assets and interest rate sensitive liabilities have affected the Company's interest income and interest expense during the periods indicated. Information is provided on Mortgage Assets and borrowings on Mortgage Assets, only, with respect to (1) changes attributable to changes in volume (changes in volume multiplied by prior rate), (2) changes attributable to changes in rate (changes in rate multiplied by prior volume), (3) changes in interest due to both rate and volume, and (4) the net change.

	Year Ended December 31, 1999 over 1998			
	Volume	**Rate**	**Rate/ Volume**	**Net Change**
		(in thousands)		
Increase/(decrease) in:				
Subordinated securities collateralized by mortgages	$ (182)	$ 1,593	$ (26)	$ 1,385
Subordinated securities collateralized by other loans	274	(107)	(42)	125
Total investment securities available-for-sale	92	1,486	(68)	1,510
Loan receivables:				
CMO collateral	(9,211)	(9,621)	917	(17,915)
Mortgage loans held-for-investment	(11,025)	(4,317)	3,314	(12,028)
Finance receivables:				
Affiliated	(14,483)	(215)	98	(14,600)
Non-affiliated	(288)	(180)	5	(463)
Total finance receivables	(14,771)	(395)	103	(15,063)
Total Loan Receivables	(35,007)	(14,333)	4,334	(45,006)
Change in interest income on Mortgage Assets	(34,915)	(12,847)	4,266	(43,496)
CMO borrowings	(8,989)	(2,355)	247	(11,097)
Reverse repurchase agreements–mortgages	(18,324)	(1,056)	486	(18,894)
Borrowings on secured by securities available-for-sale	—	—	686	686
Reverse repurchase agreements–securities	(697)	(10)	5	(702)
Change in interest expense on borrowings on Mortgage Assets	(28,010)	(3,421)	1,424	(30,007)

Change in net interest income	$ (6,905)	$ (9,426)	$ 2,842	$ (13,489)

	Year Ended December 31, 1998 over 1997			
	Volume	Rate	Rate/ Volume	Net Change
	(in thousands)			
Increase/(decrease) in:				
Subordinated securities collateralized by mortgages	$ 3,772	$ (47)	$ (25)	$ 3,700
Subordinated securities collateralized by other loans	(106)	(237)	24	(319)
Total investment securities available-for-sale	3,666	(284)	(1)	3,381
Loan receivables:				
CMO collateral	47,248	(1,630)	(1,574)	44,044
Mortgage loans held-for-investment	(2,640)	3,025	(547)	(162)
Finance receivables:				
Affiliated	—	(121)	(12)	(133)
Non-affiliated	5,778	(180)	(347)	5,251
Total finance receivables	5,778	(301)	(359)	5,118
Total Loan Receivables	50,386	1,094	(2,480)	49,000
Change in interest income on Mortgage Assets	54,052	810	(2,481)	52,381
CMO borrowings	35,470	2,111	2,063	39,644
Reverse repurchase agreements–mortgages	1,602	929	27	2,558
Reverse repurchase agreements–securities	(134)	—	(2)	(136)
Change in interest expense on borrowings on Mortgage Assets	36,938	3,040	2,088	42,066
Change in net interest income	$ 17,114	$ (2,230)	$ (4,569)	$ 10,315

Hedging

The Company conducts certain hedging activities in connection with both its Long-Term Investment Operations and its Conduit Operations.

Long-Term Investment Operations. To the extent consistent with IMH's election to qualify as a REIT, the Company follows a hedging program intended to protect against interest rate changes and to enable the Company to earn net interest income in periods of generally rising, as well as declining or static, interest rates. Specifically, the Company's hedging program is formulated with the intent to offset the potential adverse effects resulting from (1) interest rate adjustment limitations on its mortgage loans and securities backed by mortgage loans, and (2) the differences between the interest rate adjustment indices and interest rate adjustment periods of its adjustable rate mortgage loans and mortgage-backed securities secured by such loans and related borrowings. As part of its hedging program, the Company also monitors on an ongoing basis the prepayment risks that arise in fluctuating interest rate environments.

The Company's hedging program encompasses a number of procedures. First, the Company structures its commitments so that the mortgage loans purchased will have interest rate adjustment indices and adjustment periods that, on an aggregate basis, correspond as closely as practicable to the interest rate adjustment indices and interest rate adjustment periods of the anticipated financing source. In addition, the Company structures its borrowing agreements to have a range of different maturities (although substantially all have maturities of less than one year). As a result, the Company adjusts the average maturity of its borrowings on an ongoing basis by changing the mix of maturities as borrowings come due and are renewed. In this way, the Company minimizes any differences between interest rate adjustment periods of mortgage loans and related borrowings that may occur due to prepayments of mortgage loans or other factors.

The Company, based on market conditions, may purchase interest rate caps to limit or partially offset adverse changes in interest rates associated with its borrowings. In a typical interest rate cap agreement, the cap purchaser makes an initial lump sum cash payment to the cap seller in exchange for the seller's promise to make cash payments to

the purchaser on fixed dates during the contract term if prevailing interest rates exceed the rate specified in the contract. In this way, the Company generally hedges as much of the interest rate risk arising from lifetime rate caps on its mortgage loans and from periodic rate and/or payment caps as the Company determines is in the best interest of the Company, given the cost of such hedging transactions and the need to maintain IMH's status as a REIT. Such periodic caps on the Company's mortgage loans may also be hedged by the purchase of mortgage derivative securities. Mortgage derivative securities can be effective hedging instruments in certain situations as the value and yields of some of these instruments tend to increase as interest rates rise and tend to decrease in value and yields as interest rates decline, while the experience for others is the converse. The Company intends to limit its purchases of mortgage derivative securities to investments that qualify as Qualified REIT Assets or Qualified Hedges so that income from such investments will constitute qualifying income for purposes of the 95% and 75% gross income tests. To a lesser extent, the Company, through its Conduit Operations, may enter into interest rate swap agreements, buy and sell financial futures contracts and options on financial futures contracts and trade forward contracts as a hedge against future interest rate changes; however, the Company will not invest in these instruments unless the Company is exempt from the registration requirements of the Commodity Exchange Act or otherwise comply with the provisions of that Act. The REIT provisions of the Internal Revenue Code of 1986, as amended (the "Code"), may restrict the Company's ability to purchase certain instruments and may severely restrict the Company's ability to employ other strategies. In all it's hedging transactions, the Company intends to deal only with counterparties that the Company believes are sound credit risks. At December 31, 1999 and 1998, the Company had $422.0 million and none, in notional amount, of interest rate caps and interest rate swaps, respectively.

Conduit Operations. In conducting its Conduit Operations, IFC is subject to the risk of rising mortgage interest rates between the time it commits to purchase mortgage loans at a fixed price and the time it sells or securitizes those mortgage loans. To mitigate this risk, IFC enters into transactions designed to hedge interest rate risks, which may include mandatory and optional forward selling of mortgage loans or mortgage-backed securities, interest rate caps, floors and swaps, and buying and selling of futures and options on futures. The nature and quantity of these hedging transactions are determined by the management of IFC based on various factors, including market conditions and the expected volume of mortgage loan purchases.

Forward Contracts

IFC sells mortgage-backed securities through forward delivery contracts with major dealers in such securities. At December 31, 1999 and 1998, IFC had $110.0 million and $46.0 million, respectively, in outstanding commitments to sell mortgage loans through mortgage-backed securities. These commitments allow IFC to enter into mandatory commitments when IFC notifies the investor of its intent to exercise a portion of the forward delivery contracts. IFC was not obligated under mandatory commitments to deliver loans to such investors at December 31, 1999 and 1998. The credit risk of forward contracts relates to the counterparties' ability to perform under the contract. IFC evaluates counterparties based on their ability to perform prior to entering into any agreements.

Futures Contracts

IFC sells future contracts against five and ten-year Treasury notes with major dealers in such securities. At December 31, 1999 and 1998, IFC had $10.0 million and none, respectively, in outstanding commitments to sell Treasury notes which expire within 90 days.

Options

In order to protect against changes in the value of mortgage loans held for sale, IFC may sell call or buy put options on U.S. Treasury bonds and mortgage-backed securities. IFC generally sells call or buys put options to hedge against adverse movements of interest rates affecting the value of its mortgage loans held for sale. The risk in writing a call option is that IFC gives up the opportunity for profit if the market price of the mortgage loans increases and the option is exercised. IFC also has the additional risk of not being able to enter into a closing transaction if a liquid secondary market does not exist. The risk of buying a put option is limited to the premium IFC paid for the put option. IFC had written option contracts with an outstanding principal balance of $20.0 million and $25.0 million at December 31, 1999 and 1998, respectively.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The information required by this Item 8 is incorporated by reference to Impac Mortgage Holdings, Inc.'s Consolidated Financial Statements and Independent Auditors' Report beginning at page F-1 of this Form 10-K.

ITEM 9. DISAGREEMENTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The information required by this Item 10 is hereby incorporated by reference to Impac Mortgage Holdings, Inc.'s definitive proxy statement, to be filed pursuant to Regulation 14A within 120 days after the end of Impac Mortgage Holdings, Inc.'s 1999 fiscal year.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this Item 11 is hereby incorporated by reference to Impac Mortgage Holdings, Inc.'s definitive proxy statement, to be filed pursuant to Regulation 14A within 120 days after the end of Impac Mortgage Holdings, Inc.'s 1999 fiscal year.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The information required by this Item 12 is hereby incorporated by reference to Impac Mortgage Holdings, Inc.'s definitive proxy statement, to be filed pursuant to Regulation 14A within 120 days after the end of Impac Mortgage Holdings, Inc.'s 1999 fiscal year.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information required by this Item 13 is hereby incorporated by reference to Impac Mortgage Holdings, Inc.'s definitive proxy statement, to be filed pursuant to Regulation 14A within 120 days after the end of Impac Mortgage Holdings, Inc.'s 1999 fiscal year.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

(a) All schedules have been omitted because they are either not applicable, not required or the information required has been disclosed in the Consolidated Financial Statements and related Notes to Consolidated Financial Statements at page F-1, or otherwise included in this Form 10-K.

(b) Reports on Form 8-K—None

(c) Exhibits

Exhibit Number	Description
3.1	Charter of the Registrant (incorporated by reference to the corresponding exhibit number to the Registrant's Registration Statement on Form S-11, as amended (File No. 33-96670), filed with the Securities and Exchange Commission on September 7, 1995).
3.1(a)	Certificate of correction of the Registrant (incorporated by reference to exhibit 3.1(a) of the Registrant's 10-K for the year ended December 31, 1998).
3.1(b)	Articles of Amendment of the Registrant (incorporated by reference to exhibit 3.1(b) of the Registrant's 10-K for the year ended December 31, 1998).
3.1(c)	Articles of Amendment for change of name to Charter of the Registrant (incorporated by reference to exhibit number 3.1(a) of the Registrant's Current Report on Form 8-K, filed February 11, 1998).
3.1(d)	Articles Supplementary and Certificate of Correction for Series A Junior Participating Preferred Stock of the Registrant (incorporated by reference to exhibit 3.1(d) of the Registrant's 10-K for the year ended December 31, 1998).
3.1(e)	Articles Supplementary for Series B 10.5% Cumulative Convertible Preferred Stock of the Registrant (incorporated by reference to exhibit 3.1b of the Registrant's Current Report on Form 8-K, filed December 23, 1998).
3.1(f)	Articles Supplementary for Series C 10.5% Cumulative Convertible Preferred Stock of the Registrant.
3.1(g)	Certificate of Correction for Series C Preferred Stock of the Registrant.
3.2	Bylaws of the Registrant, as amended and restated (incorporated by reference to the corresponding exhibit number of the Registrant's Quarterly Report on Form 10-Q for the period ending March 31, 1998).
4.1	Form of Stock Certificate of the Company (incorporated by reference to the corresponding exhibit number to the Registrant's Registration Statement on Form S-11, as amended (File No. 33-96670), filed with the Securities and Exchange Commission on September 7, 1995).
4.2	Rights Agreement between the Registrant and BankBoston, N.A. (incorporated by reference to exhibit 4.2 of the Registrant's Registration Statement on Form 8-A as filed with the Securities and Exchange Commission on October 14, 1998).
4.2(a)	Amendment No. 1 to Rights Agreement between the Registrant and BankBoston, N.A. (incorporated by reference to exhibit 4.2(a) of the Registrant's Registration Statement on Form 8-A/A as filed with the Securities and Exchange Commission on December 23, 1998).

4.3 Form of Series B 10.5% Cumulative Convertible Preferred Stock Certificate (incorporated by reference to exhibit 4.9 of the Registrant's Current Report on Form 8-K, filed December 23, 1998).

4.4 Form of Series C 10.5% Cumulative Convertible Preferred Stock Certificate.

4.5 Indenture between the Registrant and IBJ Whitehall Bank & Trust Company, dated March 29, 1999 (incorporated by reference to exhibit a(11) of the Registrant's Form 8-K filed on April 9, 1999).

4.6 First Supplemental Indenture to Indenture between the Registrant and IBJ Whitehall Bank & Trust Company, dated March 29, 1999 (incorporated by reference to exhibit a(12) of the Registrant's Form 8-K filed on April 9, 1999).

10.1 1995 Stock Option, Deferred Stock and Restricted Stock Plan, as amended and restated (incorporated by reference to exhibit 10.1 of the Registrant's Quarterly Report on Form 10-Q for the period ending March 31, 1998).

10.2 Form of Indemnity Agreement between the Registrant and its Directors and Officers (incorporated by reference to exhibit 10.4 to the Registrant's Registration Statement on Form S-11, as amended (File No. 33-96670), filed with the Securities and Exchange Commission on September 7, 1995).

10.3 Form of Tax Agreement between the Registrant and Imperial Credit Industries, Inc. (incorporated by reference to exhibit 10.5 to the Registrant's Registration Statement on Form S-11, as amended (File No. 33-96670), filed with the Securities and Exchange Commission on September 7, 1995).

10.4(a) Sublease, dated February 12, 1997, between the Registrant and Imperial Credit Industries, Inc. regarding Santa Ana Heights facility (incorporated by reference to exhibit 10.5(a) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1997).

10.4(b) Sublease Amendment, dated July 24, 1997, between the Registrant and Imperial Credit Industries, Inc. (incorporated by reference to exhibit 10.5(b) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1997).

10.4(c) Sublease Amendment, dated February 6, 1998, between the Registrant and Imperial Credit Industries, Inc. (incorporated by reference to exhibit 10.5(c) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 1997).

10.5 Form of Amended and Restated Employment Agreement with ICI Funding Corporation (incorporated by reference to exhibit 10.8 to the Registrant's Quarterly Report on Form 10-Q, as amended, for the quarter ended June 30, 1998).

10.5(a) List of Officers and terms relating to Form of Amended and Restated Employment Agreement (incorporated by reference to exhibit 10.8(a) to the Registrant's Quarterly Report on Form 10-Q, as amended, for the quarter ended June 30, 1998).

10.5(b) Form of Amendment No. 1 to Amended and Restated Employment Agreement with Impac Funding Corporation (incorporated by reference to exhibit 10.1(a) of the Registrant's Current Report on Form 8-K, filed June 2, 1998).

10.5(c) List of Officers and terms relating to Form of Amendment No. 1 to the Amended and Restated Employment Agreement with Impac Funding Corporation (incorporated by reference to exhibit 10.1(b) of the Registrant's Current Report of Form 8-K, filed June 2, 1998).

10.6 Form of Loan Purchase and Administrative Services Agreement between the Registrant and Impac Funding Corporation (incorporated by reference to exhibit 10.9 to the Registrant's Registration Statement on Form S-11, as amended (File No. 33-96670), filed with the Securities and Exchange Commission on September 7,1995).

10.7 Dividend Reinvestment and Stock Purchase Plan (incorporated by reference to Exhibit 4 to, and the prospectus included in, the Registrant's Registration Statement on Form S-3/A (File No. 333-52335), as filed with the Securities and Exchange Commission on September 4, 1998).

10.8 Servicing Agreement effective November 11, 1995 between the Registrant and Impac Funding Corporation (incorporated by reference to exhibit 10.14 to the Registrant's Registration Statement on Form S-11, as amended (File No. 333-04011), filed with the Securities and Exchange Commission on May 17, 1996).

10.9 Impac Mortgage Holdings, Inc. 1996 Stock Option Loan Plan (incorporated by reference to exhibit 10.15 to the Registrant's Form 10-K for the year ended December 31, 1996).

10.10 Real Estate Purchase, Sale and Escrow Agreement by and between TW/BRP Dove, LLC and IMH/ICH Dove Street, LLC, dated as of August 25, 1997 (incorporated by reference to exhibit 10.16 to the Registrant's Quarterly Report on Form 10-Q, as amended, for the quarter ended June 30, 1997).

10.10(a) Contract of Sale between the Registrant and Impac Commercial Holdings, Inc. (incorporated by reference to exhibit 10.11(a) of the Registrant's 10-K for the year ended December 31, 1998).

10.11 Termination Agreement, effective December 19, 1997, between the Registrant, Impac Funding Corporation, Imperial Credit Industries, Inc. and Imperial Credit Advisors, Inc. and Joseph R. Tomkinson, William S. Ashmore and Richard J. Johnson (incorporated by reference to exhibit 10.18 to the Registrant's Current Report on Form 8-K, as amended, dated December 19, 1997).

10.12 Services Agreement, dated December 29, 1997, between the Registrant, Impac Funding Corporation and Imperial Credit Advisors, Inc. (incorporated by reference to exhibit 10.19 to the Registrant's Current Report on Form 8-K, as amended, dated December 19, 1997).

10.13 Registration Rights Agreement, dated December 29, 1997, between Registrant and Imperial Credit Advisors, Inc. (incorporated by reference to exhibit 10.20 to the Registrant's Current Report on Form 8- K, as amended, dated December 19, 1997).

10.14 Sales Agency Agreement between the Registrant and PaineWebber, Incorporated, dated May 12, 1998 (incorporated by reference to exhibit 1.1 of the Registrant's Current Report on Form 8-K, filed June 2, 1998).

10.15 Lease dated June 1, 1998 regarding Dove Street facilities (incorporated by reference to exhibit 10.17 of the Registrant's 10-K for the year ended December 31, 1998).

10.16 Employment Letter between Impac Funding Corporation and Ronald Morrison dated May 28, 1998 (incorporated by reference to exhibit 10.18 of the Registrant's 10-K for the year ended December 31, 1998).

10.17 Note dated June 30, 1999 between the Registrant and Impac Funding Corporation.

21.1 Subsidiaries of the Registrant (incorporated by reference to exhibit 21.1 of the Registrant's 10-K for the year ended December 31, 1998).

23.1 Consent of KPMG LLP regarding the Registrant.

23.2 Consent of KPMG LLP regarding Impac Funding Corporation.

24 Power of Attorney (included on signature page).

27 Financial Data Schedule.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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, in the City of Newport Beach, State of California, on the 17th day of March, 2000.

IMPAC MORTGAGE HOLDINGS, INC.

by /s/ JOSEPH R. TOMKINSON
Joseph R. Tomkinson
Chairman of the Board
and Chief Executive Officer

We, the undersigned directors and officers of Impac Mortgage Holdings, Inc., do hereby constitute and appoint Joseph R. Tomkinson and Richard J. Johnson, or either of them, our true and lawful attorneys and agents, to do any and all acts and things in our name and behalf in our capacities as directors and officers and to execute any and all instruments for us and in our names in the capacities indicated below, which said attorneys and agents, or either of them, may deem necessary or advisable to enable said corporation to comply with the Securities Exchange Act of 1934, as amended, and any rules, regulations, and requirements of the Securities and Exchange Commission, in connections with this report, including specifically, but without limitation, power and authority to sign for us or any of us in our names and in the capacities indicated below, any and all amendments to this report, and we do hereby ratify and confirm all that the said attorneys and agents, or either of them, shall do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Act of 1934, this report has been signed by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ JOSEPH R. TOMKINSON Joseph R. Tomkinson	Chairman of the Board and Chief Executive Officer (Principal Executive Officer)	March 17, 2000
/s/ RICHARD J. JOHNSON Richard J. Johnson	Chief Financial Officer (Principal Financial and Accounting Officer)	March 17, 2000
/s/ JAMES WALSH James Walsh	Director	March 17, 2000
/s/ FRANK P. FILIPPS Frank P. Filipps	Director	March 17, 2000
/s/ STEPHAN R. PEERS Stephan R. Peers	Director	March 17, 2000
/s/ WILLIAM S. ASHMORE William S. Ashmore	Director	March 17, 2000

INDEPENDENT AUDITORS' REPORT AND CONSOLIDATED FINANCIAL STATEMENTS

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INDEPENDENT AUDITORS' REPORT

The Board of Directors
Impac Mortgage Holdings, Inc.:

We have audited the accompanying consolidated balance sheets of Impac Mortgage Holdings, Inc. and subsidiaries as of December 31, 1999 and 1998, and the related consolidated statements of operations and comprehensive earnings (loss), changes in stockholders' equity and cash flows for each of the years in the three-year period ended December 31, 1999. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Impac Mortgage Holdings, Inc. and subsidiaries as of December 31, 1999 and 1998, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 1999 in conformity with generally accepted accounting principles.

KPMG LLP

Orange County, California
January 31, 2000, except as to Note T to
the consolidated financial statements,
which is as of February 29, 2000.

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(dollar amounts in thousands, except share data)

	At December 31, 1999	At December 31, 1998
ASSETS		
Cash and cash equivalents	$ 20,152	$ 33,876
Investment securities available-for-sale	93,206	93,486
Loan Receivables:		
CMO collateral	949,677	1,161,220
Finance receivables	197,119	311,571
Mortgage loans held-for-investment	363,435	20,627
Allowance for loan losses	(4,029)	(6,959)
Net loan receivables	1,506,202	1,486,459
Investment in Impac Funding Corporation	17,372	13,246
Due from affiliates	14,500	17,904
Accrued interest receivable	11,209	10,039
Other real estate owned	8,820	8,456
Other assets	3,969	2,038
Total assets	$ 1,675,430	$ 1,665,504
LIABILITIES AND STOCKHOLDERS' EQUITY		
CMO borrowings	$ 850,817	$ 1,072,316
Reverse repurchase agreements	539,687	323,625
Borrowings secured by investment securities available-for-sale	31,333	—
11% senior subordinated debentures	6,691	—
Accrued dividends payable	3,570	12,129
Due to affiliates	2,945	2,670
Other liabilities	1,543	3,158
Total liabilities	1,436,586	1,413,898
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, $0.01 par value; 6,300,000 shares authorized; none issued and outstanding at December 31, 1999 and 1998	—	—
Series A junior participating preferred stock, $0.01 par value; 2,500,000 shares authorized; none issued and outstanding at December 31, 1999 and 1998, respectively	—	—
Series B 10.5% cumulative convertible preferred stock, $0.01 par value; liquidation value $30,000; 1,200,000 shares authorized; and 1,200,000 issued and outstanding at December 31, 1999 and 1998, respectively	12	12
Common stock, $0.01 par value; 50,000,000 shares authorized; 21,400,906 and 24,557,657 shares issued and outstanding at December 31, 1999 and 1998, respectively	214	246
Additional paid-in capital	327,632	342,945
Accumulated other comprehensive loss	(7,579)	(1,736)
Notes receivable from common stock sales	(905)	(918)
Net accumulated deficit:		
Cumulative dividends declared	(93,080)	(79,176)
Retained earnings (accumulated deficit)	12,550	(9,767)
Net accumulated deficit	(80,530)	(88,943)
Total stockholders' equity	238,844	251,606
Total liabilities and stockholders' equity	$ 1,675,430	$ 1,665,504

See accompanying notes to consolidated financial statements.

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE EARNINGS (LOSS)

(in thousands, except per share data)

	For the year ended December 31,		
	1999	**1998**	**1997**
INTEREST INCOME:			
Mortgage Assets	$ 117,224	$ 160,720	$ 108,339
Other interest income	2,234	2,938	1,194
Total interest income	119,458	163,658	109,533
INTEREST EXPENSE:			
CMO borrowings	65,212	76,309	36,665
Reverse repurchase agreements	23,229	42,139	39,717
Other borrowings	1,354	3,247	195
Total interest expense	89,795	121,695	76,577
Net interest income	29,663	41,963	32,956
Provision for loan losses	5,547	4,361	6,843
Net interest income after provision for loan losses	24,116	37,602	26,113
NON-INTEREST INCOME:			
Equity in net earnings (loss) of Impac Funding Corporation	4,292	(13,876)	8,316
Equity in net loss of Impac Commercial Holdings, Inc.	—	(998)	(239)
Loss on sale of loans	—	(3,111)	—
Servicing fees	1,370	1,929	980
Gain on sale of securities	93	427	648
Other income	1,147	2,090	621
Total non-interest income	6,902	(13,539)	10,326
NON-INTEREST EXPENSE:			
Professional services	2,678	2,243	1,117
(Gain) loss on sale of other real estate owned	2,159	1,707	(433)
Write-down on investment securities available-for-sale	2,037	14,132	—
General and administrative and other expense	1,343	2,320	836
Personnel expense	484	518	331
Loss on equity investment of Impac Commercial Holdings, Inc.	—	9,076	—
Advisory fees	—	—	6,242
Termination agreement expense	—	—	44,375
Total non-interest expense	8,701	29,996	52,468
Net earnings (loss)	22,317	(5,933)	(16,029)
Less: Cash dividends on cumulative convertible preferred stock	(3,290)	—	—
Net earnings available to common stockholders	19,027	(5,933)	(16,029)
Other comprehensive earnings (loss):			
Unrealized gains (losses) on securities:			
Unrealized holding gains (losses) arising during period	(5,538)	7,395	(2,657)
Less: Reclassification of losses included in income	(305)	(4,015)	—
Net unrealized gains (losses) arising during period	(5,843)	3,380	(2,657)
Comprehensive earnings (loss)	$ 16,474	$ (2,553)	$ (18,686)
Net earnings (loss) per share—basic	$ 0.83	$ (0.25)	$ (0.99)
Net earnings (loss) per share—diluted	$ 0.76	$ (0.25)	$ (0.99)

See accompanying notes to consolidated financial statements.

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

	Number of Preferred Shares Outstanding	Preferred Stock	Number of Common Shares Outstanding	Common Stock	Additional Paid-In Capital	Accumulated Other Comprehensive Earnings (Loss)	Notes Receivable Common Stock Sales	Cumulative Dividends Declared	Retained Earnings (Accumulated Deficit)	Total Stockholders' Equity
Balance, December 31, 1996	—	$ —	9,400,000	$ 94	$ 135,521	$ (2,459)	$ (720)	$ (15,441)	$ 12,195	$ 129,190
Dividends declared ($1.68 per share)	—	—	—	—	—	—	—	(28,486)	—	(28,486)
Net proceeds from public stock offerings	—	—	3,229,906	32	83,088	—	—	—	—	83,120
Proceeds from DRSPP	—	—	1,062,844	11	24,678	—	—	—	—	24,689
Proceeds from exercise of stock options	—	—	72,966	1	935	—	—	—	—	936
Payments on notes receivable from common stock sales	—	—	—	—	—	—	(610)	—	—	(610)
Stock issued for termination of management agreement	—	—	2,009,310	20	35,017	—	—	—	—	35,037
Gain on sale of ICH preferred stock	—	—	—	—	3,840	—	—	—	—	3,840
3-for-2 stock split	—	—	6,770,638	67	(67)	—	—	—	—	—
Net loss, 1997	—	—	—	—	—	—	—	—	(16,029)	(16,029)
Other comprehensive loss	—	—	—	—	—	(2,657)	—	—	—	(2,657)
Balance, December 31, 1997	—	—	22,545,664	225	283,012	(5,116)	(1,330)	(43,927)	(3,834)	229,030
Dividends declared ($1.46 per share)	—	—	—			—	—	(35,249)	—	(35,249)
Net proceeds from preferred stock offering	1,200,000	12	—	—	28,758	—	—	—	—	28,770
Proceeds from DRSPP	—	—	1,758,493	18	27,822	—	—	—	—	27,840
Proceeds from SES Program	—	—	245,700	3	3,245	—	—	—	—	3,248
Proceeds from exercise of stock options	—	—	7,800	—	108	—	—	—	—	108
Payments on notes receivable from common stock sales	—	—	—	—	—	—	412	—	—	412
Net loss, 1998	—	—	—	—	—	—	—	—	(5,933)	(5,933)
Other comprehensive earnings	—	—	—	—	—	3,380	—	—	—	3,380
Balance, December 31, 1998	1,200,000	12	24,557,657	246	342,945	(1,736)	(918)	(79,176)	(9,767)	251,606
Dividends declared ($0.48 per common share)	—	—	—	—	—	—	—	(10,614)	—	(10,614)
Dividends declared on preferred shares	—	—	—	—	—	—	—	(3,290)	—	(3,290)
Proceeds from DRSPP	—	—	216,156	—	946	—	—	—	—	946
Repurchase of common stock	—	—	(2,013,400)	(19)	(9,841)	—	—	—	—	(9,860)
Exchange of Common Stock for senior subordinated debt	—	—	(1,359,507)	(13)	(6,418)	—	—	—	—	(6,431)
Payments on notes receivable from common stock sales	—	—	—	—	—	—	13	—	—	13
Net earnings, 1999	—	—	—	—	—	—	—	—	22,317	22,317
Other comprehensive loss	—	—	—	—	—	(5,843)	—	—	—	(5,843)
Balance, December 31, 1999	1,200,000	$ 12	21,400,906	$ 214	$ 327,632	$ (7,579)	$ (905)	$ (93,080)	$ 12,550	$ 238,844

See accompanying notes to consolidated financial statements.

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	For the year ended December 31,		
	1999	1998	1997
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net earnings (loss)	$ 22,317	$ (5,933)	$ (16,029)
Adjustments to reconcile net earnings (loss) to net cash provided by operating activities:			
Equity in net (earnings) loss of Impac Funding Corporation	(4,292)	13,876	(8,316)
Equity in net loss of Impac Commercial Holdings, Inc.	—	998	239
Provision for loan losses	5,547	4,361	6,843
Buyout of management agreement	—	—	44,375
Depreciation and amortization	—	355	75
Amortization of CMO premiums and deferred securitization costs	18,593	14,358	7,105
Loss on sale of ICH common stock	—	9,076	—
Net change in accrued interest receivable	(1,170)	4,973	(7,749)
Write-down of investment securities available-for-sale	2,037	14,132	—
Gain (loss) on sale of REO	(2,159)	(1,707)	433
Gain on sale of investment securities available-for-sale	(93)	(427)	(648)
Net change in other assets and liabilities	15,059	3,105	(10,707)
Net cash provided by operating activities	55,839	57,167	15,621
CASH FLOWS FROM INVESTING ACTIVITIES:			
Net change in CMO collateral	178,519	(385,568)	(306,705)
Net change in finance receivables	113,969	221,100	(161,533)
Net change in mortgage loans held-for-investment	(352,603)	225,301	(269,681)
Purchase of investment securities available-for-sale	(18,295)	(66,329)	(12,555)
Sale of investment securities available-for-sale	3,803	15,801	10,285
Issuance of note to IFC	(14,500)	—	—
Principal reductions on investment securities available-for-sale	6,985	13,727	(3,244)
Purchase of equity in residual interests in securitizations from IFC	—	—	(9,338)
Proceeds from sale of other real estate owned	18,027	11,777	7,902
Purchase of premises and equipment	—	(2,489)	(3,941)
Contributions to Impac Funding Corporation	—	—	(8,910)
Contributions to Impac Commercial Holdings, Inc.	—	—	(15,123)
Dividends from investment in Impac Commercial Holdings, Inc.	—	1,812	739
Net cash provided by (used in) investing activities	(64,095)	35,132	(772,104)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net change in reverse repurchase agreements	247,395	(431,934)	397,843
Proceeds from CMO borrowings	298,076	768,012	521,746
Repayment of CMO borrowings	(519,575)	(437,602)	(254,352)
Proceeds from preferred stock	—	28,770	—
Proceeds from public stock offerings, net	—	—	83,120
Dividends paid	(22,463)	(33,491)	(23,285)
Repurchase of common stock	(9,860)	—	—
Proceeds from sale of common stock issued through DRSPP and SES	946	31,088	24,689
Proceeds from exercise of stock options	—	108	936
Advances to purchase common stock	13	412	(610)
Net cash provided by (used in) financing activities	(5,468)	(74,637)	750,087

See accompanying notes to consolidated financial statements.

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS—(continued)

(in thousands)

Net change in cash and cash equivalents	(13,724)	17,662	(6,396)
Cash and cash equivalents at beginning of year	33,876	16,214	22,610
Cash and cash equivalents at end of year	$ 20,152	$ 33,876	$ 16,214
SUPPLEMENTARY INFORMATION:			
Interest paid	$ 88,989	$ 122,904	$ 73,053
NON-CASH TRANSACTIONS:			
Exchange of Common Stock for senior subordinated debt	$ 6,431	$ —	$ —
Sale of Impac Commercial Holdings common stock	—	6,099	—
Sale of Dove St. building and other assets in exchange for debt	—	6,000	—
Accumulated other comprehensive gain (loss)	(5,843)	3,380	(2,657)
Gain on sale of subsidiary preferred stock	—	—	3,840
Issuance of stock to ICAI for termination of management agreement	—	—	35,037
Transfer of loans held-for-investment to other real estate owned	1,318	7,924	6,780
Transfer of CMO collateral to other real estate owned	14,431	4,883	6,451
Dividends declared and unpaid	3,570	12,129	10,371

See accompanying notes to consolidated financial statements.

Note A—Summary of Business and Significant Accounting Policies

1. Financial Statement Presentation

The operations of the Company have been presented in the consolidated financial statements for the three-year period ended December 31, 1999 and include the financial results of Impac Mortgage Holdings, Inc. (IMH), IMH Assets Corporation (IMH Assets) and Impac Warehouse Lending Group (IWLG) as stand-alone entities and the financial results of IMH's equity interest in net earnings (loss) in Impac Funding Corporation (IFC) as a stand-alone entity. The financial results of IMH's equity interest in net loss in Impac Commercial Holdings, Inc. (ICH) as a stand-alone entity are presented in the consolidated financial statements for the two-year period ended December 31, 1998.

The Company is entitled to 99% of the earnings or losses of IFC through its ownership of all of the non-voting preferred stock of IFC. As such, the Company records its investment in IFC using the equity method. Under this method, original investments are recorded at cost and adjusted by the Company's share of earnings or losses. Certain officers and directors of the Company own all of the common stock of IFC and are entitled to 1% of the earnings or losses of IFC. Gain on the sale of loans or securities by IFC to IMH are deferred and accreted for gain on sale over the estimated life of the loans or securities using the interest method.

All significant intercompany balances and transactions with IMH's consolidated subsidiaries have been eliminated in consolidation. Interest income on affiliated short-term advances, due from affiliates, has been earned at the rate of 8.00% per annum. Interest expense on affiliated short-term borrowings, due to affiliates, has been incurred at the rate of 8.00% per annum. Costs and expenses of affiliates have been charged to ICH in proportion to services provided per the submanagement agreement between FIC Management Inc. (FIC), an affiliate of Fortress Partners LP (Fortress), IMH and IFC, not to exceed an annual fee of $250,000. Certain amounts in the prior periods' consolidated financial statements have been reclassified to conform to the current presentation.

Management of the Company has made a number of 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 financial statements in conformity with generally accepted accounting principles. Actual results could differ from those estimates.

2. Cash and Cash Equivalents

For purposes of the consolidated statements of cash flows, cash and cash equivalents consists of cash and money market mutual funds. The Company considers investments with maturities of three months or less at date of acquisition to be cash equivalents.

3. Investment Securities Available-for-Sale

The Company classifies investment and mortgage-backed securities as held-to-maturity, available-for-sale, and/or trading securities. Held-to-maturity investment and mortgage-backed securities are reported at amortized cost, available-for-sale securities are reported at fair value with unrealized gains and losses as a separate component of stockholders' equity, and trading securities are reported at fair value with unrealized gains and losses reported in earnings. The Company's investment securities are held as available-for-sale, reported at fair value with unrealized gains and losses reported as a separate component of stockholders' equity. Gains and losses on sale of investment securities available-for-sale are based on the specific identification method. As the Company qualifies as a Real Estate Investment Trust (REIT), and no income taxes are paid, the unrealized gains and losses are reported gross in stockholders' equity. Premiums or discounts obtained on investment securities are accreted or amortized to interest income over the estimated life of the investment securities using the interest method. Such investments may subject the Company to credit, interest rate and/or prepayment risk.

The Company determines the decline in fair value to be other than temporary if the present value of estimated future cash flows discounted at a risk-free rate is less than the amortized cost basis of the security. In that event, the cost basis of the security is written down to fair value as a new cost basis and the amount of the write down is included in earnings.

IMH purchases a large portion of the residuals created by IFC's securitizations recorded at IFC as a result of the sale of mortgage loans through securitizations. IFC sells a portfolio of mortgage loans to a special purpose entity that has been established for the limited purpose of buying and reselling the mortgage loans. IFC then transfers the same mortgage loans to a special purpose entity or owners trust (the Trust). The Trust issues interest-bearing asset-backed securities generally in an amount equal to the aggregate principal balance of the mortgage loans. IFC typically sells these certificates at face value and without recourse except that representations and warranties customary to the mortgage banking industry are provided by IFC. IMH or other investors purchase these certificates from the Trust and the proceeds from the sale of the certificates are used as consideration to purchase the underlying mortgage loans from the Company. In addition, IFC may provide a credit enhancement for the benefit of the investors in the form of additional collateral held by the Trust. The over-collateralization account is required to be maintained at specified levels.

To determine the value of the securities, the Company must estimate future rates of prepayments, prepayment penalties to be received by the Company, delinquencies, defaults and default loss severity and their impact on estimated cash flows. At December 31, 1999, the Company used a 0.50% to 9% constant default rate estimate with a 1% to 20% severity resulting in loss estimates of 0% to 5%. These estimates are based on historical loss data for comparable loans. The Company estimates prepayments by evaluating historical prepayment performance of comparable mortgage loans and trends in the industry. At December 31, 1999, the Company used a constant prepayment assumption of 12% to 31% to estimate the prepayment characteristics of the underlying collateral.

The Company determines the estimated fair value of the residuals by discounting the expected cash flows using a discount rate, which it believes is commensurate with the risks involved. At December 31, 1999, the Company used a weighted average discount rate of approximately 12.7%.

4. CMO Collateral and Mortgage Loans Held-for-Investment

The Company purchases non-conforming mortgage loans to be held as long-term investment or as Collateral Mortgage Obligations (CMOs) collateral. Mortgage loans held-for-investment and CMO collateral are recorded at cost at the date of purchase. Mortgage loans held-for-investment and CMO collateral include various types of fixed and adjustable rate loans secured by mortgages on single-family residential real estate properties and fixed rate loans secured by second trust deeds on single-family residential real estate properties. Premiums and discounts, which may result from the purchase or acquisition of mortgage loans in excess of the outstanding principal balance, are amortized to interest income over their estimated lives using the interest method as an adjustment to the carrying amount of the loan. Prepaid securitization costs related to the issuance of CMOs are amortized to interest expense over their estimated lives using the interest method. Mortgage loans are continually evaluated for collectibility and, if appropriate, the mortgage loans may be placed on non-accrual status, generally when the mortgage is 90 days past due, and previously accrued interest reversed from income. Other than temporary impairment in the carrying value of mortgage loans held-for-investment, if any, will be recognized as a reduction to current operations.

5. Finance Receivables

Finance receivables represent transactions with customers, including affiliated companies, involving residential real estate lending. As a warehouse lender, the Company is a secured creditor of the mortgage bankers and brokers to which it extends credit and is subject to the risks inherent in that status including, the risk of borrower default and bankruptcy. Any claim of the Company as a secured lender in a bankruptcy proceeding may be subject to adjustment and delay. The Company's finance receivables represent warehouse lines of credit with mortgage banking companies collateralized by

mortgage loans on single family residences. Finance receivables are stated at the principal balance outstanding. Interest income is recorded on the accrual basis in accordance with the terms of the loans. Finance receivables are continually evaluated for collectibility and, if appropriate, the receivable is placed on non-accrual status, generally when 90 days past due. Future collections of interest income are included in interest income or applied to the loan balance based on an assessment of the likelihood that the loans will be repaid.

6. Allowance for Loan Losses

The Company maintains an allowance for losses on mortgage loans held-for-investment, collateral for CMOs, and finance receivables at an amount which it believes is sufficient to provide adequate protection against future losses in the mortgage loans portfolio. The allowance for losses is determined primarily on management's judgment of net loss potential including specific allowances for known impaired loans, changes in the nature and volume of the portfolio, value of the collateral and current economic conditions that may affect the borrowers' ability to pay. A provision is recorded for loans deemed to be uncollectible thereby increasing the allowance for loan losses. Subsequent recoveries on mortgage loans previously charged off are credited back to the allowance.

7. Premises and Equipment

Premises and equipment are stated at cost, less accumulated depreciation or amortization. Depreciation on premises and equipment is recorded using the straight-line method over the estimated useful lives of individual assets (three to twenty years).

8. CMO Borrowings

The Company issues CMOs, which are primarily secured by non-conforming mortgage loans on single-family residential real property, as a means of financing its Long-Term Investment Operations. CMOs are carried at their outstanding principal balances including accrued interest on such obligations. For accounting and tax purposes, mortgage loans financed through the issuance of CMOs are treated as assets of the Company and the CMOs are treated as debt of the Company. Each issue of CMOs is fully payable from the principal and interest payments on the underlying mortgage loans collateralizing such debt and any investment income on such collateral. The Company's CMOs typically are structured as one-month London interbank offered rate (LIBOR) "floaters" and fixed-rate securities with interest payable monthly. The maturity of each class of CMO is directly affected by the rate of principal prepayments on the related CMO collateral. Each CMO series is also subject to redemption according to specific terms of the respective indentures. As a result, the actual maturity of any class of a CMO series is likely to occur earlier than the stated maturities of the underlying mortgage loans.

9. Income Taxes

IMH operates so as to qualify as a REIT under the requirements of the Internal Revenue Code (the Code). Requirements for qualification as a REIT include various restrictions on ownership of IMH's stock, requirements concerning distribution of taxable income and certain restrictions on the nature of assets and sources of income. A REIT must distribute at least 95% of its taxable income to its stockholders, the distribution of which 85% must be distributed within the taxable year in order to avoid the imposition of an excise tax and the remaining balance may extend until timely filing of its tax return in its subsequent taxable year. Qualifying distributions of its taxable income are deductible by a REIT in computing its taxable income. If in any tax year IMH should not qualify as a REIT, it would be taxed as a corporation and distributions to the stockholders would not be deductible in computing taxable income. If IMH were to fail to qualify as a REIT in any tax year, it would not be permitted to qualify for that year and the succeeding four years.

10. Net Earnings (Loss) per Share

Basic net earnings per share are computed on the basis of the weighted average number of shares outstanding for the year divided by net earnings for the year. Diluted net earnings per share are computed on the basis of the weighted average number of shares and common equivalent shares outstanding for the year divided by net earnings for the year.

11. Recent Accounting Pronouncements

In June 1998, the Financial Accounting Standards Board (FASB) issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" (SFAS 133). SFAS 133 establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, (collectively referred to as derivatives) and for hedging activities. It requires that an entity recognizes all derivatives as either assets or liabilities in the statement of financial position and measures those instruments at fair value. If certain conditions are met, a derivative may be specifically designated as (a) a hedge of the exposure to changes in the fair value of a recognized asset or liability or an unrecognized firm commitment, (b) a hedge of the exposure to variable cash flows of a forecasted transaction, or (c) a hedge of the foreign currency exposure of a net investment in a foreign operation, an unrecognized firm commitment, an available-for-sale security, or a foreign-currency-denominated forecasted transaction. This statement is effective for all fiscal quarters of fiscal years beginning after June 15, 1999. SFAS 133 was amended by SFAS No. 137, which allows deferral of SFAS 133 for all fiscal quarters of fiscal years beginning after July 15, 2000. Management is evaluating the impact of implementation of SFAS 133 on the Company's financial position and results of operations.

Note B—Investment Securities Available-for-Sale

The Company's mortgage-backed securities are primarily secured by conventional, one-to-four family mortgage loans. The yield to maturity on each security depends on, among other things, the rate and timing of principal payments, including prepayments, repurchases, defaults and liquidations, the pass-through rate, and interest rate fluctuations. The Company's interest in these securities is subordinated so that, in the event of a loss, payments to senior certificate holders will be made before the Company receives its payments. At December 31, 1999 and 1998, the Company's investment securities available-for-sale included $87.6 million and $88.1 million, respectively, of subordinated securities collateralized by mortgages and $5.6 million and $5.4 million, respectively, of subordinated securities collateralized by other loans.

In connection with the issuance of REMICs by IFC during the years ended December 31, 1999 and 1998 of $360.1 million and $907.5 million, respectively, IMH purchased $18.3 million and $23.4 million, respectively, of securities as regular interests and none and $37.2 million, respectively, of "interest-only" securities. During 1999, the Company recorded $3.7 million in discounts, at the time of purchase, in connection with the purchase of the mortgage-backed securities.

The amortized cost and estimated fair value of mortgage-backed securities available-for-sale and other collateralized securities available-for-sale are summarized as follows:

	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss	Estimated Fair Value
		(in thousands)		
At December 31, 1999:				
Mortgage-backed securities	$ 94,986	$ 1,235	$ 8,007	$ 88,214
Other collateralized securities	5,633	—	641	4,992
	$ 100,619	$ 1,235	$ 8,648	$ 93,206
At December 31, 1998:				
Mortgage-backed securities	$ 89,825	$ 2,560	$ 4,296	$ 88,089
Other collateralized securities	5,397	—	—	5,397
	$ 95,222	$ 2,560	$ 4,296	$ 93,486

Note C—Mortgage Loans Held-for-Investment

Mortgage loans held-for-investment include various types of adjustable rate loans secured by mortgages on single-family residential real estate properties and fixed rate loans secured by second trust deeds on single-family residential real estate properties. During the years ended December 31, 1999 and 1998, IMH purchased $638.3 million and $866.7 million, respectively, of mortgage loans from IFC. At December 31, 1999 and 1998, approximately 64% and 39%, respectively, of mortgage loans held-for-investment were collateralized by properties located in California. Mortgage loans held-for-investment consisted of the following:

	At December 31, 1999	At December 31, 1998
	(in thousands)	
Adjustable rate loans secured by single-family residential real estate	$ 335,609	$ 20,145
Fixed rate loans secured by second trust deeds on single-family residential real estate	25,785	—
Unamortized net premiums on mortgage loans	2,041	482
	$ 363,435	$ 20,627

At December 31, 1999, 1998 and1997, there were $8.3 million, $7.3 million and $6.4 million, respectively, of mortgage loans held-for-investment which were not accruing interest due to the delinquent nature of the mo rtgage loans. If interest on such loans had been accrued for the years ended December 31, 1999, 1998 and 1997, interest income would have increased by $538,000, $724,000 and $299,000, respectively.

Note D—CMO Collateral

CMO collateral includes various types of fixed and adjustable rate loans secured by mortgages on single-family residential real estate properties and fixed rate loans secured by second trust deeds on single-family residential real estate properties. During the years ended December 31, 1999 and 1998, $298.1 million and $768.0 million, respectively, of CMOs were issued and collateralized by $316.2 million and $788.2 million, respectively, of mortgage loans. At December 31, 1999 and 1998, approximately 43% of CMO collateral was collateralized by properties located in California. At December 31, 1999 and 1998, the underlying principal balance of mortgages supporting CMO borrowings of $850.8 million and $1.1 billion, respectively, represented approximately $827.3 million and $1.1 billion, respectively, of adjustable and fixed rate mortgage loans with varying grade quality and approximately $81.7 million and $24.2 million, respectively, of second mortgage loans.

Collateral for CMOs consisted of the following:

	At December 31,	
	1999	1998
	(in thousands)	
Adjustable and fixed rate loans secured by single-family residential real estate	$ 827,268	$ 1,085,388
Fixed rate loans secured by second trust deeds on single-family residential real estate	81,718	24,189
Unamortized net premiums on loans	28,798	39,369
Securitization expenses	11,893	12,274
	$ 949,677	$ 1,161,220

Note E—Finance Receivables

The terms of IWLG's affiliated warehouse lines are based on Bank of America's prime rate, which was 8.50% and 7.75% as of December 31, 1999 and 1998, respectively, with advance rates between 90% and 98% of the fair value of the mortgage loans outstanding. The terms of IWLG's non-affiliated warehouse lines, including the maximum warehouse line amount and interest rate, are determined based upon the financial strength, historical performance and other qualifications of the borrower. The warehouse lines have maturities that range from on-demand to one year and are generally collateralized by mortgages on single-family residential real estate.

At December 31, 1999 and 1998, the Company had $1.4 billion and $813.1 million, respectively, of warehouse lines of credit available to 49 and 32 borrowers, respectively, of which $197.1 million and $311.6 million, respectively, was outstanding. IWLG finances its Warehouse Lending Operations through reverse repurchase agreements and equity. Finance receivables consisted of the following:

	At December 31,	
	1999	1998
	(in thousands)	
Due from IFC	$ 66,125	$ 192,900
Due from Impac Commercial Capital Corporation	—	3,642
Due from Walsh Securities, Inc.	48	1,544
Due from Impac Lending Group (ILG)	1,243	—
Due from other mortgage banking companies	129,703	113,485
	$ 197,119	$ 311,571

Note F—Allowance for loan losses

Activity for allowance for loan losses was as follows:

	For the year ended December 31,		
	1999	1998	1997
		(in thousands)	
Balance, beginning of year	$ 6,959	$ 5,129	$ 4,384
Provision for loan losses	5,547	4,361	6,843
Charge-offs, net of recoveries	(7,152)	(1,711)	(4,748)
Loss on sale of delinquent loans	(1,325)	(820)	(1,350)
Balance, end of year	$ 4,029	$ 6,959	$ 5,129

Note G—Reverse repurchase agreements

The Company entered into reverse repurchase agreements with major brokerage firms to finance its Warehouse Lending Operations and to fund the purchase of mortgage loans and mortgage-backed securities. Mortgage loans and mortgage-backed securities underlying reverse repurchase agreements are delivered to dealers that arrange the transactions. The Company's reverse repurchase agreements are uncommitted lines, which may be withdrawn at any time by the lender, with interest rates that range from one-month LIBOR plus 0.85% to 2.00% depending on the type of collateral provided.

Prior to October of 1999, the Company used reverse repurchase agreements to fund the purchase of its mortgage-backed securities and to provide the Company additional working capital. In October of 1999, the Company repaid its borrowings of reverse repurchase agreements secured by mortgage-backed securities with proceeds from the re-securitization of a portion of its mortgage-backed securities portfolio (see Note I-Borrowings Secured by Investment Securities Available-for-Sale). The Company's interest expense on reverse repurchase agreements for the years ended December 31, 1999 and 1998 was $22.5 million and $42.1 million, respectively. The following tables set forth information regarding the Company's reverse repurchase agreements (in thousands):

	At December 31, 1999					
	Type of Collateral	Committed	Commitment Amount	Reverse Repurchase Liability	Underlying Collateral	Maturity Date
Lender 1	Mortgages	No	$ 536,112	$ 536,112	$ 547,408	N/A
Lender 2	Mortgages	No	3,575	3,575	3,956	N/A
			$ 539,687	$ 539,687	$ 551,364	

	At December 31, 1998					
	Type of Collateral	Committed	Commitment Amount	Reverse Repurchase Liability	Underlying Collateral	Maturity Date
Lender 1	Mortgages	No	$ 299,567	$ 299,567	$ 313,338	N/A
Lender 2	Securities	Yes	10,017	10,017	30,595	12/29/99
Lender 3	Securities	Yes	7,876	7,876	18,578	1/21-3/26/99(1)
Lender 4	Securities	Yes	3,632	3,632	12,189	1/05/99(1)
Lender 5	Securities	Yes	2,533	2,533	8,715	1/15/99(1)
			$ 323,625	$ 323,625	$ 383,415	

(1) Upon expiration, these reverse repurchase agreements were renewed.

At December 31, 1999 and December 31, 1998, reverse repurchase agreements includes accrued interest payable of $3.7 million and $2.0 million, respectively. The following table presents certain information on reverse repurchase agreements, excluding accrued interest payable:

	For the year ended December 31,	
	1999	1998
	(dollars in thousands)	
Maximum month-end outstanding balance	$ 569,862	$ 912,444
Average balance outstanding	346,556	631,537
Weighted average rate	6.51%	6.67%

Note H—CMO Borrowings

The Company's CMOs are guaranteed for the holders by a mortgage loan insurer giving the CMOs the highest rating established by a nationally recognized rating agency. Each issue of CMOs is fully payable from the principal and interest payments on the underlying mortgage loans collateralizing such debt, any cash or other collateral required to be pledged as a condition to receiving the desired rating on the debt, and any investment income on such collateral. The Long-Term Investment Operations earns the net interest spread between the interest income on the mortgage loans securing the CMOs and the interest and other expenses associated with the CMO financing. Interest expense includes the amortization of securitization costs. The net interest spread may be directly impacted by prepayment levels of the underlying mortgage loans, and, to the extent each CMO class has variable rates of interest, may be affected by changes in short-term interest rates. Variable rate CMOs are typically structured as one-month LIBOR "floaters." Interest on variable and fixed rate CMOs is payable to the certificate holders monthly. For the years ended December 31, 1999, 1998 and 1997, interest expense on CMO borrowings was $65.2 million, $76.3 million $36.7 million, respectively. The following table sets forth CMOs issued by the Company, CMOs outstanding as of December 31, 1999 and 1998, and certain interest rate information (dollars in millions):

Issue Date	Issuance Name	Issuance Amount	CMOs Outstanding as of 12/31/99	CMOs Outstanding as of 12/31/98	Range of Fixed Interest Rates	Range of Interest Rate Margins Over One-Month LIBOR	Interest Rate Margin Adjustment Date	Range of Interest Rate Margins After Adjustment Date
4/22/96	Fund America Investors Trust V	$ 296.3	$ 41.7	$ 79.2	N/A	0.50%	6/2003	1.00%
8/27/96	Impac CMB Trust Series 1996-1	259.8	37.1	64.6	N/A	0.32%	10/2003	1.32%
5/22/97	Impac CMB Trust Series 1997-1	348.0	68.5	168.9	N/A	0.22%	7/2004	0.44%
12/10/97	Impac CMB Trust Series 1997-2	173.7	43.6	120.9	N/A	0.26% to 1.30%	1/2005	0.52% to 2.60%
1/27/98	Impac CMB Trust Series 1998-1	362.8	179.6	283.7	6.65% to 7.25%	N/A	N/A	N/A
3/24/98	Impac CMB Trust Series 1998-2	220.2	120.7	190.4	6.70% to 7.25%	N/A	N/A	N/A
6/23/98	Impac CMB Trust Series 1998-3	185.0	94.8	161.6	N/A	0.18% to 1.24%	7/2005	0.36% to 2.48%
2/23/99	Impac CMB Trust Series 1999-1	183.1	154.4	—	10.00% to 18.25%	2.88% to 7.40%	N/A	N/A
6/24/99	Impac CMB Trust Series 1999-2	115.0	108.3	—	N/A	3.00% to 8.50%	N/A	N/A
		2,143.9	848.7	1,069.3				
	Accrued interest	—	2.1	3.0				
		$ 2,143.9	$ 850.8	$ 1,072.3				

Note I—Borrowings Secured by Investment Securities Available-for-Sale

In October 1999, the Company completed a re-securitization of its investment securities available-for-sale, which raised additional cash liquidity for the Company of approximately $23.4 million after repaying reverse repurchase agreements collateralized by the investment securities available-for-sale. As of December 31, 1999, there was $31.3 million

outstanding on the borrowings, which were secured by $49.6 of mortgage-backed securities available-for-sale. The outstanding borrowings are principal only notes issued at a discount. The notes represent senior or subordinated interests in trust funds primarily consisting of a pool of mortgage loans and are non-recourse obligations of the Company. The terms of the notes are dependent on the cash flows from the underlying certificates.

Note J—Senior Subordinated Debentures

In March 1999, certain stockholders of the Company exchanged 1,359,507 shares of their common stock, at an average price of $5.70 per share, for 11% senior subordinated debentures due to mature on February 15, 2004. The debentures are unsecured obligations of the Company subordinated to all indebtedness of the Company's subsidiaries. The debentures bear interest at 11% per annum from their date of issuance, payable quarterly, commencing May 15, 1999, until the debentures are paid in full. The debentures mature on February 15, 2004, at which the date may be extended once by the Company to a date not later than May 15, 2004, provided that the Company satisfies certain conditions. Commencing on February 15, 2001, the debentures are redeemable, at the Company's option, in whole at any time or in part from time to time, at the principal amount to be redeemed plus accrued and unpaid interest thereon to the redemption date.

Note K—Segment Reporting

The basis for the Company's segments is to separate its entities as follows: segments that derive income from investment in long-term Mortgage Assets, segments that derive income by providing short-term financing and segments that derive income from the purchase and sale or securitization of mortgage loans.

The Company internally reviews and analyzes its segments as follows:

- The Long-Term Investment Operations, conducted by IMH and IMH Assets, invests primarily in non-conforming residential mortgage loans and mortgage-backed securities secured by or representing interests in such loans and in second mortgage loans.
- The Warehouse Lending Operations, conducted by IWLG, provides warehouse and repurchase financing to affiliated companies and to approved mortgage banks, most of which are correspondents of IFC, to finance mortgage loans.
- The Conduit Operations, conducted by IFC, purchases non-conforming mortgage loans and second mortgage loans from its network of third party correspondents and other sellers.

The following table shows the Company's reporting segments as of and for the year ended December 31, 1999 (in thousands):

	Long-Term Investment Operations	Warehouse Lending Operations	(b) Other	(c) Eliminations	Consolidated
Balance Sheet Items:					
CMO collateral	$ 949,677	$ —	$ —	$ —	$ 949,677
Total assets	1,545,283	588,448	2,945	(461,246)	1,675,430
Total stockholders' equity	294,852	48,684	—	(104,692)	238,844
Income Statement Items:					
Interest income	91,965	31,998	21	(4,526)	119,458
Interest expense	72,704	21,612	5	(4,526)	89,795
Equity in IFC (a)	4,292	—	—	—	4,292
Net earnings	6,828	9,939	41	5,509	22,317

The following table shows the Company's reporting segments as of and for the year ended December 31, 1998 (in thousands):

	Long-Term Investment Operations	Warehouse Lending Operations	(b) Other	(c) Eliminations	Consolidated
Balance Sheet Items:					
CMO collateral	$ 1,161,220	$ —	$ —	$ —	$ 1,161,220
Total assets	1,410,019	338,365	3,418	(86,298)	1,665,504
Total stockholders' equity	277,868	38,745	615	(65,622)	251,606
Income Statement Items:					
Interest income	121,271	57,500	358	(15,471)	163,658
Interest expense	95,095	41,903	168	(15,471)	121,695
Depreciation and amortization	11	—	344	—	355
Equity in IFC (a)	(13,876)	—	—	—	(13,876)
Net earnings (loss)	(6,369)	15,057	560	(15,181)	(5,933)

The following table shows the Company's reporting segments as of and for the year ended December 31, 1997 (in thousands):

	Long-Term Investment Operations	Warehouse Lending Operations	(b) Other	(c) Eliminations	Consolidated
Balance Sheet Items:					
CMO collateral	$ 794,893	$ —	$ —	$ —	$ 794,893
Total assets	1,287,200	766,844	19,872	(321,104)	1,752,812
Total stockholders' equity	255,729	23,688	3,889	(54,276)	229,030
Income Statement Items:					
Interest income	72,092	52,643	—	(15,202)	109,533
Interest expense	53,607	38,172	—	(15,202)	76,577
Depreciation and amortization	10	—	65	—	75
Equity in IFC (a)	8,316	—	—	—	8,316
Net earnings (loss)	(38,279)	14,527	27	7,696	(16,029)

(a) The Conduit Operations is accounted for using the equity method and is an unconsolidated subsidiary of the Company.
(b) Primarily includes the operations of Dove, of which the Company owned a 50% interest, and account reclassifications.
(c) Elimination of intersegment balance sheet and income statement items.

Note L—Fair Value of Financial Instruments

The estimated fair value amounts have been determined by IMH using available market information and appropriate valuation methodologies, however, considerable judgment is necessarily required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented are not necessarily indicative of the amounts IMH could realize 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.

	December 31, 1999		December 31, 1998	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Assets	(in thousands)			
Cash and cash equivalents	$ 20,152	$ 20,152	$ 33,876	$ 33,876
Investment securities available-for-sale	93,206	93,206	93,486	93,486
CMO collateral	949,677	938,784	1,161,220	1,185,188
Finance receivables	197,119	197,119	311,571	311,571
Mortgage loans held-for-investment	363,435	366,066	20,627	20,627
Due from affiliates	14,500	14,500	17,904	17,904
Interest rate caps	1,925	2,091	—	—
Liabilities				
CMO borrowings, excluding accrued interest	848,756	844,852	1,069,323	1,071,375
Reverse-repurchase agreements, excluding accrued interest	535,990	535,990	321,667	321,667
Borrowings secured by investment securities available-for-sale	31,333	34,393	—	—
Senior subordinated debentures	6,691	6,198	—	—
Due to affiliates	2,945	2,945	2,670	2,670
Short-term commitments to extend credit	—	—	—	—

The fair value estimates as of December 31, 1999 and 1998 are based on pertinent information available to management as of that date. Although management is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively revalued for purposes of these consolidated financial statements since those dates and, therefore, current estimates of fair value may differ significantly from the amounts presented.

The following describes the methods and assumptions used by IMH in estimating fair values:

Cash and Cash Equivalents

Fair value approximates carrying amounts as these instruments are demand deposits and money market mutual funds and do not present unanticipated interest rate or credit concerns.

Investment Securities Available-for-Sale

Fair value is estimated using a bond model, which incorporates certain assumptions such as prepayment, yield and losses.

CMO Collateral

Fair value is estimated based on quoted market prices from dealers and brokers for similar types of mortgage loans.

Finance Receivables

Fair value approximates carrying amounts due to the short-term nature of the assets and do not present unanticipated interest rate or credit concerns.

Mortgage Loans Held-for-Investment

Fair value is estimated based on estimates of proceeds the Company would receive from the sale of the underlying collateral of each loan.

Due From / To Affiliates

Fair value approximates carrying amount because of the short-term maturity of the liabilities and does not present unanticipated interest rate or credit concerns.

CMO Borrowings

Fair value of fixed rate borrowings is estimated based on the use of a bond model, which incorporates certain assumptions such as prepayment, yield and losses. Fair value of variable rate borrowings approximate carrying amount because of the variable interest rate nature of the borrowings.

Reverse Repurchase Agreements

Fair value approximates carrying amounts due to the short-term nature of the liabilities and do not present unanticipated interest rate or credit concerns.

Borrowings Secured by Investment Securities Available-for-Sale

Fair value is estimated based on quoted market prices from dealers or brokers.

Senior Subordinated Debt

Fair value is estimated based on quoted market price from dealers or brokers.

Interest Rate Caps

Fair value is estimated based on quoted market prices from dealers or brokers.

Short-term Commitments to Extend Credit

The Company does not collect fees associated with its warehouse lines of credit. Accordingly, these commitments do not have an estimated fair value.

Note M—Employee Benefit Plans

Profit Sharing and 401(k) Plan

The Company does not have its own 401(K) or profit sharing plan. As such, employees of the Company participate in Imperial Credit Industries, Inc's. (ICII) 401(K) plan. Under ICII's 401(K) plan, employees of the Company may contribute up to 14% of their salaries. The Company will match 50% of the first 4% of employee contributions. Additional Company contributions may be made at the discretion of the Company. The Company's matching and discretionary contributions were not material for any period presented.

Note N—Related Party Transactions

Related Party Cost Allocations

In 1995, IMH entered into a services agreement with ICII under which ICII provided various services to the Company, including data processing, human resource administration, general ledger accounts, check processing, remittance processing and payment of accounts payable. ICII charged fees for each of the services based upon usage. As part of the services provided, ICII provided the Company with insurance coverage and self-insurance programs, including health insurance. This services agreement was replaced with a new ICAI services agreement in December 1997, in connection with termination of the Company's management agreement with ICAI. Pursuant to the services agreement with ICAI, ICAI provides the Company certain human resource administration and data and phone communication services. The charge to the Company for insurance coverage is based upon a pro rata portion of the costs to ICII for its various policies. Total charges to the Company for the years ended December 31, 1999, 1998 and 1997 were $11,000, $13,000, and $8,000, respectively.

During 1999 and 1998, IMH and IWLG were allocated data processing, executive and operations management, and accounting services that IFC incurred during the normal course of business per the Company's submanagement agreement with RAI Advisors Inc. (RAI). IFC, through RAI, charged IMH and IWLG for management and operating services based upon usage which management believes was reasonable. In May 1999, the submanagement agreement with RAI was terminated and IFC entered into a new submanagement agreement with FIC Management, Inc., pursuant to which IFC provides services to Impac Commercial Holdings, Inc. (ICH). Prior to the submanagement agreement with RAI and after RAI was terminated, IMH and IWLG were allocated data processing, executive and operations management, and accounting services that IFC incurred during the normal course of business. IFC charged IMH and IWLG for management and operating services based upon usage which management believes was reasonable. Total cost allocations charged by IFC to IMH and IWLG for the years ended December 31, 1999, 1998 and 1997 were $1.2 million, $968,000 and $385,000, respectively.

Lease Agreement: IMH and IFC entered into with ICH a premises operating sublease agreement (see Note O—Commitments and Contingencies) to rent approximately 74,000 square feet of office space in Newport Beach, California, for a ten-year term, which expires in May 2008. IMH and IFC pay monthly rental expenses and allocate the cost to subsidiaries and affiliated companies on the basis of square footage occupied.

The majority of occupancy charges incurred were paid by IFC as most of the Company's employees are employed by the Conduit Operations. Total rental expense for the years ended December 31, 1999, 1998 and 1997 were $1.1 million, $1.3 million and $396,000, of which $1.0 million, $1.2 million and $385,000 was paid by IFC, respectively.

Credit Arrangements - Current

IWLG maintains a warehouse financing facility with IFC. Advances under such warehouse facilities bear interest at Bank of America's prime rate. As of December 31, 1999 and 1998, finance receivables outstanding to IFC were $66.1 million and $192.9 million, respectively. Interest income recorded by IWLG related to finance receivables due from IFC for the years ended December 31, 1999, 1998, and 1997, was $18.4 million, $32.7 million, and $33.5 million, respectively.

IWLG maintains a warehouse financing facility with ILG. Advances under such warehouse facilities bear interest at prime plus 1.50% rate. As of December 31, 1999, amounts outstanding on ILG's warehouse line with IWLG were $1.2 million. Interest expense recorded by ILG related to warehouse lines with IWLG for the year ended December 31, 1999 was $293,000. There were no borrowings prior to 1999.

IWLG maintains a warehouse financing facility with WSI, a firm affiliated with James Walsh, a Director of the Company. Advances under the line of credit bear interest at a rate determined at the time of each advance. As of

December 31, 1999, 1998 and 1997, finance receivables outstanding to WSI were $48,000, $798,000 and $5.9 million, respectively. Interest income recorded by IWLG related to finance receivables due from WSI for the years ended December 31, 1999, 1998 and 1997 was $729,000, $699,000 and $255,000, respectively.

During the normal course of business, the Company may advance or borrow funds on a short-term basis with affiliated companies. Advances to affiliates are reflected as "Due from affiliates", while borrowings are reflected as "Due to affiliates" on the Company's balance sheet. These short-term advances and borrowings bear interest at a fixed rate of 8.00% per annum. As of December 31, 1999 and 1998, due from affiliates was none and $17.9 million, respectively. Interest income recorded by the Company related to short-term advances due from affiliates for the years ended December 31, 1999 and 1998 was $835,000 and $2.4 million, respectively. As of December 31, 1999 and 1998, due to affiliates was $2.9 million and $2.7 million, respectively. Interest expense recorded by the Company related to short-term borrowings due to affiliates for the years ended December 31, 1999 and 1998 was $399,000 and $2.7 million, respectively.

Indebtedness of Management. In connection with the exercise of stock options by certain directors and employees of the Company, the Company made loans secured by the related stock. The loans were made for a five-year term with a current interest rate of 5.63%. Interest on the loans is payable quarterly upon receipt of the dividend payment and the interest rate is set annually by the compensation committee. At each dividend payment date, 50% of excess quarterly stock dividends, after applying the dividend payment to interest due, is required to reduce the principal balance outstanding on the loans. The interest rate on these loans adjusts annually at the discretion of the Board of Directors. As of December 31, 1999 and 1998, total notes receivable from common stock sales was $905,000 and $918,000, respectively. Interest income recorded by the Company related to the loans for the years ended December 31, 1999, 1998 and 1997 was $41,000, $60,000 and $68,000, respectively.

Credit Arrangements - Expired

IMH maintained an uncommitted warehouse line agreement with ICCC. The margins on the warehouse line agreement were at 8% of the fair market value of the collateral provided. Advances under such warehouse facilities bore interest at Bank of America's prime rate. As of December 31, 1999 and 1998, finance receivables outstanding to ICCC were none and $3.6 million, respectively. Interest income recorded by IMH related to finance receivables due from ICCC for the years ended December 31, 1999 and 1998 was $93,000 and $785,000, respectively.

IMH entered into a revolving credit arrangement with a commercial bank which was an affiliate of ICII, whereby IMH could borrow up to maximum amount of $10.0 million for general working capital needs. The revolving credit agreement was converted to a reverse repurchase agreement in October 1998. Advances under the reverse repurchase agreement were at an interest rate of LIBOR plus 2.00%, with interest paid monthly. As of December 31, 1999 and 1998, IMH's outstanding borrowings under the reverse repurchase arrangement were none and $10.0 million, respectively. Interest expense recorded by IMH for the year ended December 31, 1999 and 1998 related to such advances was $348,000 and $202,000, respectively.

During 1997, IWLG extended loans of $5.1 million to WSI at rates ranging from prime plus 2% per annum to prime plus 4% per annum. As of December 31, 1999 and 1998, WSI had an aggregate of none and $746,000, respectively, outstanding on the loans. Interest income recorded by IWLG related to loans due from WSI for the years ended December 31, 1999 and 1998 was $20,000 and $254,000, respectively.

Termination of Management Agreement: As part of the Company's termination agreement of its Management Agreement with ICAI, the Company purchased the equity in residual interests in securitizations from IFC for $9.0 million and simultaneously retired IFC's borrowings with the Company for the equity in residual interests in securitizations for $9.0 million. No gain or loss on the sale of residual interests in securitizations was recorded by the Company or IFC.

Transactions with IFC

Purchase of Mortgage-Backed Securities: During the years ended December 31, 1999 and 1998, the Company purchased $22.0 million and $60.6 million, respectively, of mortgage-backed securities issued by IFC for $18.3 million and $56.1 million, respectively, net of discounts of $3.7 million and $4.5 million, respectively. IFC issued mortgage-backed securities during 1999 and 1998 in connection with its REMIC securitizations.

Purchase of Mortgage Loans: During the years ended December 31, 1999 and 1998, the Company purchased from IFC mortgage loans having a principal balance of $637.4 million and $842.9 million, respectively. The loans were purchased with premiums of $877,000 and $23.9 million, respectively. Servicing rights on all mortgages purchased by IMH were retained by IFC.

Sale of Mortgage Loans: During the year ended December 31, 1999 and 1998, the Company sold to IFC mortgage loans having a principal balance of $10.8 million and $170.4 million, respectively, with premiums of $294,000 and $7.7 million, respectively.

Sale of Franchise Loans Receivables: In April 1998, IMH sold the beneficial interest in the Class A Trust Certificate for the Franchisee Loan Receivables Trust 1995-B Franchise Loans Receivables and the beneficial interest in the Class E Trust Certificate for the Franchisee Loan Receivables Trust 1996-B to IFC at carrying value which approximated fair value. No gain or loss was recorded on the sale and IMH was under no obligation to sell the securities.

Sub-Servicing Agreement: IFC acts as a servicer of mortgage loans acquired on a "servicing-released" basis by the Company in its Long-Term Investment Operations pursuant to the terms of a Servicing Agreement, which became effective on November 20, 1995. IFC subcontracts all of its servicing obligations under such loans to independent third parties pursuant to sub-servicing agreements.

Advances: During 1999, IMH advanced $14.5 million in cash to IFC at an interest rate of 9.50% per annum due June 30, 2004, in exchange for an interest only note in anticipation of the initial capitalization of the Bank and to fund the operations of IFC and other strategic opportunities deemed appropriate by IFC. Interest income recorded by IMH related to this note was $696,000.

Transactions with ICH and ICCC

Sale of Commercial Office Building: On October 27, 1998, the Company sold to ICH its remaining 50% ownership interest in a commercial office building located in Newport Beach, California for $6.0 million. After the sale of the 50% ownership interest to ICH, the Company has no ownership interest in the commercial office building.

Sale of ICH Common Stock: On October 21, 1998, ICH repurchased from IMH 937,084 shares of ICH Common Stock and 456,916 shares of ICH Class A Common Stock at a per share price of $4.375, based upon the closing sales price of the Common Stock on the AMEX on October 19, 1998, for a total repurchase of $6.1 million. The Company recorded a loss on the sale of ICH Common Stock of $9.1 million. The sale of ICH Common Stock represented 100% of IMH's ownership of ICH Common Stock.

Transactions with ICII and ICAI

Redemption of Senior Notes: On January 24, 1997, IMH redeemed ICII senior note obligations for $5.2 million, resulting in a gain of $648,000.

Termination of Management Agreement: Effective December 19, 1997, the Company terminated its Management Agreement with ICAI. A termination fee in the aggregate of $44.0 million was paid with 2,009,310 shares of the Company's common stock representing a value of $35.0 million in addition to equity in IFC's residual interest in

securitizations. In connection with the Termination Agreement, the Company entered into a Registration Rights Agreement with ICAI with regards to the 2,009,310 shares of Common Stock. IMH purchased the equity in residual interests in securitizations from IFC for $9.0 million and simultaneously retired IFC's borrowings with IMH for the equity in residual interest in securitizations of $9.0 million. No gain or loss on the sale of residual interests in securitizations was recorded by IMH or IFC. For financial accounting purposes, the termination fee was treated as a non-recurring, non-cash expense and resulted in a charge of $44.4 million to the Company's fourth quarter income.

Non-Compete Agreement and Right of First Refusal Agreement

Pursuant to the Non-Compete Agreement executed on the date of the ICH initial public offering, IFC will not acquire any commercial mortgages for a period of the earlier of nine months from the closing of the ICH initial public offering or the date upon which ICH and/or ICCC accumulates (for investment or sale) $300.0 million of commercial mortgages or commercial mortgage-backed securities. This agreement expired in March 1998.

Pursuant to a Right of First Refusal Agreement by and among IMH, IFC, ICH, ICCC and RAI, pursuant to which, in part, RAI agreed that any mortgage loan or mortgage-backed security investment opportunity which is offered to it on behalf of either ICH, IMH any affiliated REIT will first be offered to that entity whose initial primary business as described in its initial public offering documentation most closely aligns with such investment opportunity. The Right of First Refusal Agreement was terminated in May 1999.

Note O—Commitments and Contingencies

Financial Instruments with Off-Balance-Sheet Risk

IMH is a party to financial instruments with off-balance sheet risk in the normal course of business. Such instruments include short-term commitments to extend credit to borrowers under warehouse lines of credit, which involve elements of credit risk, lease commitments, interest rate cap agreements, and exposure to credit loss in the event of nonperformance by the counterparties to the various agreements associated with loan purchases. Unless noted otherwise, IMH does not require collateral or other security to support such commitments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments. The contract or notional amounts of interest rate cap agreements and forward contracts do not represent exposure to credit loss. The Company controls the credit risk of its interest rate cap agreements and forward contracts through credit approvals, limits and monitoring procedures.

Short-Term Loan Commitments

IWLG's warehouse lending program provides secured short-term non-recourse revolving financing to small-and medium-size mortgage originators and affiliated companies to finance mortgages from the closing of the loans until sold to permanent investors. As of December 31, 1999 and 1998, the Company had 49 and 32 committed lines of credit, respectively, extended in the aggregate principal amount of $1.4 billion and $813.1 million, respectively, of which $67.4 million and $198.1 million, respectively, was outstanding with affiliated companies. The Company's warehouse lines are non-recourse and IWLG can only look to the sale or liquidation of the mortgages as a source of repayment.

Lease Commitments

The Company entered into a premises operating lease for approximately 74,000 square feet of office space in Newport Beach, California which expires in May 2008. Minimum premises rental commitments under non-cancelable leases are as follows (in thousands):

Year 2000	1,812
Year 2001	1,856
Year 2002	1,901
Year 2003	1,946
Year 2004	1,990
Year 2005 and thereafter	7,132
Total Lease Commitments	$ 16,637

Rent expense associated with the premises operating lease is allocated between IMH, IWLG and IFC based on square footage. IMH and IWLG's combined portion of premises rental expense for the years ended December 31, 1999, 1998, and 1997 was $100,000, $65,000, and $11,000, respectively.

Interest Rate Cap Agreements

The Company purchases and sells, from time to time, interest rate agreements in the form of interest rate caps, interest rate floors, and other interest rate futures to attempt to mitigate interest and related risks. The Company also may use such instruments to modify the characteristics of its CMO issuance or to hedge the anticipated issuance of future liabilities or the market value of certain assets. The Company intends generally to hedge as much of the interest rate risk based on the cost of such hedging transaction and the need to maintain the Company's status as a REIT. At December 31, 1999 and 1998, the Company had $422.0 million and none, in notional amount, of interest rate caps, respectively. The carrying value of the interest rate caps was $1.9 million.

Loan Purchase Commitments

In the ordinary course of business, IFC is exposed to liability under representations and warranties made to purchasers and insurers of mortgage loans and the purchasers of servicing rights. Under certain circumstances, IFC is required to repurchase mortgage loans if there had been a breach of representations or warranties. IMH has guaranteed the performance obligation of IFC under such representation and warranties related to loans included in securitizations. However, IMH does not anticipate nonperformance by such borrowers or counterparties.

Note P—Management Contract

Effective December 19, 1997, the Company terminated its Management Agreement with ICAI. The termination fee of $44.0 million was paid with 2,009,310 shares of the Company's Common Stock in addition to other assets. During the year ended December 31, 1997, the Company paid fees to ICAI of $6.2 million.

Note Q—Stock Option Plan

The Company adopted a Stock Option, Deferred Stock and Restricted Stock Plan (the Stock Option Plan) which provides for the grant of qualified incentive stock options (ISOs), options not qualified (NQSOs) and deferred stock, restricted stock, stock appreciation, dividend equivalent rights and limited stock appreciation rights awards (Awards). The Stock Option Plan is administered by a committee of directors appointed by the Board of Directors (the Administrator). ISOs may be granted to the officers and key employees of the Company. NQSOs and Awards may be granted to the directors, officers and key employees of the Company or any of its subsidiaries, to the directors, officers

and key employees of IFC. The exercise price for any NQSO or ISO granted under the Stock Option Plan may not be less than 100% (or 110% in the case of ISOs granted to an employee who is deemed to own in excess of 10% of the outstanding Common Stock) of the fair market value of the shares of Common Stock at the time the NQSO or ISO is granted. Unless previously terminated by the Board of Directors, no options or Awards may be granted under the Stock Option Plan after August 31, 2005.

Options granted under the Stock Option Plan will become exercisable in accordance with the terms of the grant made by the Administrator. Awards will be subject to the terms and restrictions of the award made by the Administrator. The Administrator has discretionary authority to select participants from among eligible persons and to determine at the time an option or Award is granted and, in the case of options, whether it is intended to be an ISO or a NQSO, and when and in what increments shares covered by the option may be purchased. As of December 31, 1999 and 1998, options to purchase 592,098 shares and 562,500 shares, respectively, were exercisable and 525,109 shares and 462,219 shares, respectively, were reserved for future grants under the Stock Option Plan.

Option transactions for the periods shown are summarized as follows:

	For the year ended December 31,					
	1999		1998		1997	
	Number of Shares	Weighted-Average Exercise Price	Number of Shares	Weighted-Average Exercise Price	Number of Shares	Weighted-Average Exercise Price
Options outstanding at beginning of year	737,781	$ 10.06	724,675	$ 12.56	548,250	$ 9.47
Options granted	35,500	4.92	195,781	5.68	325,125	16.73
Options exercised	—	—	(7,800)	13.75	(103,700)	8.77
Options forfeited/cancelled	(98,390)	9.45	(174,875)	15.34	(45,000)	13.75
Options outstanding at end of year	674,891	$ 9.89	737,781	$ 10.06	724,675	$ 12.56

As of December 31, 1999 and 1998, total notes receivable from Common Stock sales were $905,000 and $918,000, respectively. Interest on all loans secured by the Company's Common Stock is payable quarterly upon receipt of the Company's dividend payment. At each dividend payment date, 50% of excess quarterly stock dividends, after applying the dividend payment to interest due, is required to reduce the principal balance outstanding on the loans. The interest rate on these loans adjusts annually and is set at the discretion of the Board of Directors.

During 1998, the Company made one loan totaling $30,000 to an employee of the Company that is secured by the related Common Stock in connection with the exercise of stock options under the Stock Option Plan. There were no loans made in 1999.

The following table sets forth information about fixed stock options outstanding at December 31, 1999:

	Stock Options Outstanding			Options Exercisable	
Exercise Prices	Number Outstanding	Weighted-Average Remaining Contractual Life (mos.)	Weighted-average exercise price ($)	Number Exercisable	Weighted-Average exercise price ($)
$ 4.44	144,391	3.94	$ 4.44	97,098	$ 4.44
4.56	2,500	2.72	4.56	—	—
4.69	25,000	4.65	4.69	—	—
5.75	5,500	2.15	5.75	—	—
5.81	2,500	2.57	5.81	—	—
7.50	255,000	5.66	7.50	255,000	7.50
15.42	127,500	7.08	15.42	127,500	15.42
17.58	112,500	3.81	17.58	112,500	17.58
	674,891	5.16	9.89	592,098	10.62

In November 1995, the FASB issued SFAS No. 123, "Accounting for Stock-Based Compensation" (SFAS 123). This statement establishes financial accounting standards for stock-based employee compensation plans. SFAS 123 permits the Company to choose either a new fair value based method or the current APB Opinion 25 intrinsic value based method of accounting for its stock-based compensation arrangements. SFAS 123 requires pro forma disclosures of net earnings (loss) computed as if the fair value based method had been applied in financial statements of companies that continue to follow current practice in accounting for such arrangements under Opinion 25. SFAS 123 applies to all stock-based employee compensation plans in which an employer grants shares of its stock or other equity instruments to employees except for employee stock ownership plans. SFAS 123 also applies to plans in which the employer incurs liabilities to employees in amounts based on the price of the employer's stock, i.e., stock option plans, stock purchase plans, restricted stock plans, and stock appreciation rights. The statement also specifies the accounting for transactions in which a company issues stock options or other equity instruments for services provided by nonemployees or to acquire goods or services from outside suppliers or vendors.

The Company elected to continue to apply APB Opinion 25 in accounting for its Plan and, accordingly, no compensation cost has been recognized for its stock options in the financial statements. If the Company determined its compensation cost based on the fair value, at the grant date of the stock options exercisable under SFAS 123, the Company's net earnings (loss) and net earnings (loss) per share would have decreased to the pro forma amounts indicated below (dollars in thousands, except per share data):

	For the year ended December 31,		
	1999	1998	1997
Net earnings (loss) as reported	$ 22,317	$ (5,933)	$ (16,029)
Pro forma net earnings (loss)	$ 22,308	$ (6,038)	$ (16,581)
Basic earnings (loss) per share as reported	$ 0.83	$ (0.25)	$ (0.99)
Diluted earnings (loss) per share as reported	$ 0.76	$ (0.25)	$ (0.99)
Basic pro forma earnings (loss) per share	$ 0.83	$ (0.25)	$ (1.02)
Diluted pro forma earnings (loss) per share	$ 0.76	$ (0.25)	$ (1.02)

The derived fair value of the options granted during 1999, 1998 and 1997 was approximately $1.35, $0.54 and $1.70, respectively. The fair value of options granted, which is amortized to expenses over the option vesting period in

determining the pro forma impact, is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

	For the year ended December 31,		
	1999	1998	1997
Risk-Free Interest Rate	4.98%	5.09%	5.84%
Expected Lives (in years)	3-5	3-10	3-10
Expected Volatility	0.60%	29.90%	28.50%
Expected Dividend Yield	9.50%	11.50%	9.70%

Note R—Stockholders' Equity

Pursuant to IMH's Dividend Reinvestment and Stock Purchase Plan (DRSPP or the Plan), stockholders can acquire additional shares of IMH Common Stock by reinvesting their cash dividends at a 0% to 5% discount of the average high and low market prices as reported on the AMEX on the Investment Date (as described in the Plan) to the extent shares are issued by IMH. Stockholders may also purchase additional shares of IMH Common Stock through the cash investment option at a 0% to 5% discount of the average high and low market prices as reported on the AMEX during the three trading days preceding the Investment Date. During 1999, 1998 and 1997, the Company raised capital of $946,000, $3.1 million and $24.7 million, respectively, as 216,156, 1.8 million and 1.6 million shares, respectively, of Common Stock were purchased under the Company's DRSPP. Proceeds from the sale of securities were used for working capital needs. In July of 1999, the Company suspended its DRSPP.

During 1999, the Company's Board of Directors authorized the Company to repurchase up to $10.0 million of the Company's Common Stock, $.01 par value, in open market purchases from time to time at the discretion of the Company's management; the timing and extent of the repurchases will depend on market conditions. For the year ended December 31, 1999, the Company repurchased 2.0 million shares of its Common Stock for $9.9 million. The acquired shares were canceled.

During 1999, certain stockholders of the Company exchanged 1,359,507 shares of their Common Stock for 11% senior subordinated debentures due February 15, 2004. The Debentures are unsecured obligations of the Company subordinated and subject in right of payment to all existing and future senior indebtedness of the Company and effectively subordinated to all indebtedness of the Company's subsidiaries. The Debentures bear interest at 11% per annum from their date of issuance, payable quarterly, commencing May 15, 1999, until the debentures are paid in full. The debentures mature on February 15, 2004, which date may be extended once by the Company to a date not later than May 15, 2004, provided that the Company satisfies certain conditions. Commencing on February 15, 2001, the debentures will be redeemable, at the Company's option, in whole at any time or in part from time to time, at the principal amount to be redeemed plus accrued and unpaid interest to the redemption date.

On December 22, 1998, the Company completed the sale of 1,200,000 shares of Series B 10.5% Cumulative Convertible Preferred Stock (Series B Preferred Stock) at $25.00 per share. The Series B Preferred Stock was convertible into shares of the Company's Common Stock at a conversion price of $4.95 per share. Accordingly, each share of Series B Preferred Stock was convertible into 5.050505 shares of the Company's Common Stock. The terms of the acquisition provided for a downward adjustment of the conversion price if, among other things, certain earnings levels were not attained by the Company through June 30, 1999. In February 2000, the Series B Preferred Stock was exchanged for Series C 10.5% Cumulative Convertible Preferred Stock (Series C Preferred Stock) and the conversion rate was adjusted to $4.72 per share convertible into 5.29661 shares of Common Stock or an aggregate of 6,355,932 shares of Common Stock. Dividends on the Preferred Stock accumulate from the date of issuance and are paid quarterly, in cash or the Company's Common Stock, starting April 27, 1999. The dividend rate per share is the greater of $0.65625 or the quarterly cash dividend declared on the number of shares of Common Stock into which a share of Preferred Stock is convertible. The Company is authorized to issue shares of Preferred Stock designated in one or more classes or series. The Preferred

Stock may be issued from time to time with such designations, rights and preferences as shall be determined by the Board of Directors. The Preferred Stock has a preference on dividend payments, takes priority over dividend distributions to the common stockholders.

On October 7, 1998, the Company's Board of Directors adopted a Stockholder Rights Plan in which Preferred Stock Purchase Rights were distributed as a dividend at the rate of one Right for each outstanding share of Common Stock. The dividend distribution was made on October 19, 1998 payable to stockholders of record on that date. The Rights are attached to the Company's Common Stock. The Rights will be exercisable and trade separately only in the event that a person or group acquires or announces the intent to acquire 10 percent or more of the Company's Common Stock. Each Right will entitle stockholders to buy one-hundredth of a share of a new series of junior participating Preferred Stock at an exercise price of $30.00. If the Company is acquired in a merger or other transaction after a person has acquired 10 percent or more of Company outstanding Common Stock, each Right will entitle the stockholder to purchase, at the Right's then-current exercise price, a number of the acquiring Company's common shares having a market value of twice such price. In addition, if a person or group acquires 10 percent or more of the Company's Common Stock, each Right will entitle the stockholder (other than the acquiring person) to purchase, at the Right's then-current exercise price, a number of shares of the Company's Common Stock having a market value of twice such price. Following the acquisition by a person of 10 percent or more of the Company's Common Stock and before an acquisition of 50 percent or more of the Common Stock, the Board of Directors may exchange the Rights (other than the Rights owned by such person) at an exchange ratio of one share of Common Stock per Right. Before a person or group acquires beneficial ownership of 10 percent or more of the Company's Common Stock, the Rights are redeemable for $.0001 per right at the option of the Board of Directors. The Rights will expire on October 19, 2008. The Rights distribution is not taxable to stockholders. The Rights are intended to enable all the Company stockholders to realize the long-term value of their investment in the Company.

Note S—Reconciliation of Earnings Per Share

The following table represents the computation of basic and diluted net earnings (loss) per share for the periods presented, as if all stock options, cumulative convertible preferred stock (Preferred Stock), and ICII's ownership interest in IMH were outstanding for these periods (in thousands, except per share data):

	For the year ended December 31,		
	1999	1998	1997
Numerator:			
Numerator for basic earnings per share—			
Net earnings (loss)	$ 22,317	$ (5,933)	$ (16,029)
Less: Dividends paid to preferred stockholders	(3,290)	—	—
Net earnings (loss) available to common stockholders	$ 19,027	$ (5,933)	$ (16,029)
Denominator:			
Denominator for basic earnings per share—			
Weighted average number of common shares outstanding during the period	22,824	23,914	16,267
Impact of assumed conversion of Preferred Stock	6,356	—	—
Net effect of dilutive stock options	16	—	—
Denominator for diluted earnings per share	29,196	23,914	16,267
Net earnings (loss) per share—basic	$ 0.83	$ (0.25)	$ (0.99)
Net earnings (loss) per share—diluted	$ 0.76	$ (0.25)	$ (0.99)

The antidilutive effects of stock options outstanding as of December 31, 1999, 1998 and 1997 was none, 137,105 and 210,110, respectively. The antidilutive effects of outstanding Preferred Stock as of December 31, 1999, 1998 and 1997 was none, 6,060,606 and none, respectively. Terms of the Preferred Stock acquisition provided for a downward adjustment of the conversion price if, among other things, certain earnings levels were not attained by the Company through June 30, 1999. The change in the Preferred Stock conversion price during 1999 from $5.05 per share resulted in 6,355,932 in Common Stock equivalent shares outstanding at December 31, 1999 as compared to 6,060,606 Common Stock equivalent shares outstanding at December 31, 1998

Note T—Subsequent Events

In February 2000, the Series B Preferred Stock was exchanged for Series C Preferred Stock and the conversion rate was adjusted to $4.72 per share convertible into 5.29661 shares of Common Stock or an aggregate of 6,355,932 shares of Common Stock.

Note U—Quarterly Financial Data (unaudited)

Selected quarterly financial data for 1999 follows (in thousands, except per share data):

	For the Three Months Ended,			
	December 31,	September 30,	June 30,	March 31,
Net interest income	$ 7,378	$ 5,876	$ 8,163	$ 8,246
Provision for loan losses	1,191	1,367	1,490	1,499
Non-interest income (loss)	(611)	3,784	2,019	1,710
Non-interest expense	1,639	2,062	2,738	2,262
Net earnings	3,937	6,231	5,954	6,195
Net earnings per share – diluted (1)	0.14	0.22	0.21	0.20
Dividends declared per share	0.13	0.13	0.12	0.10

Selected quarterly financial data for 1998 follows (in thousands, except per share data):

	For the Three Months Ended,			
	December 31,	September 30,	June 30,	March 31,
Net interest income	$ 9,004	$ 11,676	$ 11,517	$ 9,766
Provision for loan losses	2,262	(292)	487	1,904
Non-interest income (loss)	(10,654)	(9,534)	3,287	3,362
Non-interest expense	4,187	23,050	2,639	120
Net earnings (loss)	(8,099)	(20,616)	11,678	11,104
Net earnings (loss) per share – diluted (1)	(0.33)	(0.85)	0.49	0.48
Dividends declared per share	—	0.49	0.49	0.48

(1) Diluted earnings per share are computed independently for each of the quarters presented. Therefore, the sum of the quarterly earnings per share may not equal the total for the year.

Note V—Impac Funding Corporation

The following condensed financial information summarizes the financial condition and results of operations of Impac Funding Corporation:

Condensed Consolidated Balance Sheets
(in thousands)

	At December 31,	
	1999	1998
ASSETS		
Cash and cash equivalents	$ 8,805	$ 422
Securities available-for-sale	1,887	5,965
Securities held-for-trading	—	5,300
Mortgage loans held-for-sale	68,084	252,568
Mortgage servicing rights	15,621	14,062
Due from affiliates	4,307	9,152
Premises and equipment, net	3,575	1,978
Accrued interest receivable	48	1,896
Other assets	13,919	22,529
	$ 116,246	$ 313,872
LIABILITIES AND SHAREHOLDERS' EQUITY		
Borrowings from IWLG	$ 66,125	$ 192,900
Other borrowings	181	67,058
Due to affiliates	14,500	24,382
Deferred revenue	7,635	10,605
Accrued interest expense	843	—
Other liabilities	9,414	6,064
Total liabilities	98,698	301,009
Shareholders' equity:		
Preferred stock	18,053	18,053
Common stock	182	182
Accumulated deficit	(520)	(4,852)
Accumulated other comprehensive loss	(167)	(520)
Total shareholders' equity	17,548	12,863
	$ 116,246	$ 313,872

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(continued)

Condensed Consolidated Statements of Operations
(in thousands)

	For the year ended December 31,		
	1999	1998	1997
Net interest income:			
Total interest income	$ 21,225	$ 48,510	$ 48,020
Total interest expense	20,953	40,743	41,628
Net interest income	272	7,767	6,392
Non-interest income:			
Gain (loss) on sale of loans	27,098	(11,663)	19,414
Loan servicing income	5,221	7,071	4,109
Other income	979	(1,091)	643
Total non-interest income	33,298	(5,683)	24,166
Non-interest expense:			
Amortization of mortgage servicing rights	5,331	6,361	2,827
Write down of securities available-for-sale	4,252	—	—
Impairment of mortgage servicing rights	1,078	3,722	—
Provision for repurchases	385	367	3,148
General and administrative and other expense	14,965	14,385	10,047
Total non-interest expense	26,011	24,835	16,022
Earnings (loss) before income taxes	7,559	(22,751)	14,536
Income taxes (benefit)	3,227	(8,738)	6,136
Net earnings (loss)	$ 4,332	$ (14,013)	$ 8,400

INDEPENDENT AUDITORS' REPORT

The Board of Directors
Impac Funding Corporation:

We have audited the accompanying consolidated balance sheets of Impac Funding Corporation and subsidiary as of December 31, 1999 and 1998, and the related consolidated statements of operations and comprehensive earnings (loss), changes in shareholders' equity and cash flows for each of the years in the three-year period ended December 31, 1999. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Impac Funding Corporation and subsidiary as of December 31, 1999 and 1998, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 1999 in conformity with generally accepted accounting principles.

KPMG LLP

Orange County, California
January 31, 2000

IMPAC FUNDING CORPORATION AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

(dollar amounts in thousands)

	At December 31, 1999	At December 31, 1998
ASSETS		
Cash and cash equivalents	$ 8,805	$ 422
Securities available-for-sale	1,887	5,965
Securities held-for-trading	—	5,300
Mortgage loans held-for-sale	68,084	252,568
Mortgage servicing rights	15,621	14,062
Due from affiliates	4,307	9,152
Premises and equipment, net	3,575	1,978
Accrued interest receivable	48	1,896
Other assets	13,919	22,529
Total assets	$ 116,246	$ 313,872
LIABILITIES AND SHAREHOLDERS' EQUITY		
Borrowings from IWLG	$ 66,125	$ 192,900
Other borrowings	181	67,058
Due to affiliates	14,500	24,382
Deferred revenue	7,635	10,605
Accrued interest expense	843	—
Other liabilities	9,414	6,064
Total liabilities	98,698	301,009
Commitments and contingencies		
Shareholders' equity:		
Preferred stock, no par value; 10,000 shares authorized; 10,000 shares issued and outstanding at December 31, 1999 and 1998	18,053	18,053
Common stock, no par value; 10,000 shares authorized; 10,000 shares issued and outstanding at December 31, 1999 and 1998	182	182
Accumulated deficit	(520)	(4,852)
Accumulated other comprehensive loss	(167)	(520)
Total shareholders' equity	17,548	12,863
Total liabilities and shareholders' equity	$ 116,246	$ 313,872

See accompanying notes to consolidated financial statements.

IMPAC FUNDING CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE EARNINGS (LOSS)

(in thousands)

	For the year ended December 31,		
	1999	**1998**	**1997**
INTEREST INCOME:			
Mortgage loans held-for-sale	$ 20,352	$ 45,070	$ 42,373
Other interest income	873	3,440	5,647
Total interest income	21,225	48,510	48,020
INTEREST EXPENSE:			
Borrowings from IWLG	18,366	32,682	33,450
Other affiliated borrowings	1,673	2,020	4,618
Other borrowings	914	6,041	3,560
Total interest expense	20,953	40,743	41,628
Net interest income	272	7,767	6,392
NON-INTEREST INCOME:			
Gain (loss) on sale of loans	27,098	(11,663)	19,414
Mark-to-market loss on investment securities	—	(805)	—
Gain (loss) on sale of investment securities	—	(706)	550
Loan servicing income	5,221	7,071	4,109
Other income	979	420	93
Total non-interest income	33,298	(5,683)	24,166
NON-INTEREST EXPENSE:			
Personnel expense	7,299	8,901	6,760
Amortization of mortgage servicing rights	5,331	6,361	2,827
Write down of securities available-for-sale	4,252	—	—
General and administrative and other expense	3,417	2,516	2,228
Professional services	2,524	978	79
Occupancy expense	1,095	1,391	408
Impairment of mortgage servicing rights	1,078	3,722	—
Provision for repurchases	385	367	3,148
Data processing expense	337	387	311
Telephone and other communications	293	212	261
Total non-interest expense	26,011	24,835	16,022
Earnings (loss) before income taxes	7,559	(22,751)	14,536
Income taxes (benefit)	3,227	(8,738)	6,136
Net earnings (loss)	4,332	(14,013)	8,400
Other comprehensive earnings (loss):			
Unrealized gains (losses) on securities:			
Unrealized holding gains (losses) arising during period	329	(520)	—
Less: Reclassification of gains included in income	24	—	—
Net unrealized gains (losses) arising during period	353	(520)	—
Comprehensive earnings (loss)	$ 4,685	$ (14,533)	$ 8,400

See accompanying notes to consolidated financial statements.

IMPAC FUNDING CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(dollar amounts in thousands)

	Number of Preferred Shares	Preferred Stock	Number of Common Shares	Common Stock	Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Loss	Total Shareholders' Equity
Balance, December 31, 1996	10,000	9,143	10,000	92	761	—	9,996
Capital Contributions, 1997	—	8,910	—	90	—	—	9,000
Net earnings, 1997	—	—	—	—	8,400	—	8,400
Balance, December 31, 1997	10,000	18,053	10,000	182	9,161	—	27,396
Net loss, 1998	—	—	—	—	(14,013)	—	(14,013)
Other comprehensive loss	—	—	—	—	—	(520)	(520)
Balance, December 31, 1998	10,000	$ 18,053	10,000	$ 182	$ (4,852)	$ (520)	$ 12,863
Net earnings, 1999	—	—	—	—	4,332	—	4,332
Other comprehensive income	—	—	—	—	—	353	353
Balance, December 31, 1999	10,000	18,053	10,000	182	(520)	(167)	17,548

See accompanying notes to consolidated financial statements.

IMPAC FUNDING CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	For the year ended December 31,		
	1999	1998	1997
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net earnings (loss)	$ 4,332	$ (14,013)	$ 8,400
Adjustments to reconcile net earnings to net cash provided by (used in) operating activities:			
Provision for repurchases	385	367	3,148
Gain (loss) on sale of loans	27,098	—	—
Depreciation and amortization	6,453	7,141	3,371
Amortization of deferred revenue	(12,751)	(8,157)	(1,862)
Impairment of mortgage servicing rights	1,078	3,722	—
Net change in accrued interest receivable	1,848	2,859	(2,910)
Net change in other assets and liabilities	(6,258)	1,806	(54,291)
Net change in deferred taxes	—	(10,459)	3,172
Net change in deferred revenue	9,781	11,714	7,517
Purchase of securities held-for-trading	5,300	(5,300)	—
Write-down of investment securities	4,252	805	—
Net change in accrued interest expense	843	(5,673)	1,382
Net cash provided by (used in) operating activities	42,361	(15,188)	(32,073)
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchase of mortgage loans held-for-sale	(1,671,777)	(2,248,586)	(2,571,208)
Sale of and principal reductions on mortgage loans held-for-sale	1,827,638	2,616,170	2,284,763
Additions to mortgage servicing rights	(7,968)	(8,577)	(9,611)
Issuance of note from IMH	14,500	—	—
Sale of residual interests in securitizations	—	—	47,925
Principal reductions on residual interests in securitizations	—	—	(976)
Purchase of securities available-for-sale	(5,413)	—	(28,646)
Sale of securities available-for-sale	5,413	—	22,953
Principal reductions on securities available-for-sale	—	403	(390)
Purchase of premises and equipment	(2,719)	(970)	(1,498)
Net cash provided by (used in) investing activities	159,674	358,440	(256,688)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net change in borrowings from IWLG	(126,775)	(261,940)	127,418
Net change in other borrowings	(66,877)	(81,249)	148,307
Capital contributions	—	—	9,000
Net cash provided by (used in) financing activities	(193,652)	(343,189)	284,725
Net change in cash and cash equivalents	8,383	63	(4,036)
Cash and cash equivalents at beginning of year	422	359	4,395
Cash and cash equivalents at end of year	$ 8,805	$ 422	$ 359
SUPPLEMENTARY INFORMATION:			
Interest paid	$ 20,109	$ 44,806	$ 40,246
Taxes paid	385	5,205	2,964

See accompanying notes to consolidated financial statements.

IMPAC FUNDING CORPORATION AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note A—Summary of Business and Significant Accounting Policies

1. Business and Financial Statement Presentation

IFC is a mortgage loan conduit organization, which purchases primarily non-conforming mortgage loans from a network of third party correspondent loan originators and subsequently securitizes or sells such loans to permanent investors or IMH. On March 31, 1997, ownership of all of the Common Stock of IFC was transferred from ICII to Joseph R. Tomkinson, Chief Executive Officer of IMH and IFC, William S. Ashmore, President of IMH and IFC, and Richard J. Johnson, Chief Financial Officer of IMH and IFC, who are entitled to 1% of the earnings or losses of IFC.

The consolidated financial statements include the operations of IFC and its wholly owned subsidiary, Impac Secured Asset Corporation (collectively, IFC) and have been prepared in conformity with generally accepted accounting principles and prevailing practices within the mortgage banking industry.

All significant intercompany balances and transactions with IFC's consolidated subsidiary have been eliminated in consolidation. Interest income on affiliated short-term advances, due from affiliates, has been earned at the rate of 8% per annum. Interest expense on affiliated short-term borrowings, due to affiliates, has been incurred at the rate of 8% per annum. Certain amounts in the prior period's consolidated financial statements have been reclassified to conform to the current presentation.

Management of IFC has made a number of 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 financial statements in conformity with generally accepted accounting principles. Actual results could differ from those estimates.

2. Cash and Cash Equivalents

For purposes of the consolidated statements of cash flows, cash and cash equivalents consists of cash and money market mutual funds. IFC considers investments with maturities of three months or less at date of acquisition to be cash equivalents.

3. Gain on Sale of Loans

IFC recognizes gains or losses on the sale of loans when the sales transaction settles or upon the securitzation of the mortgage loans when the risks of ownership have passed to the purchasing party. Gains and losses may be increased or decreased by the amount of any servicing released premiums received and costs associated with the origination of mortgage loans. Gain on sale of loans or securities to IMH are deferred and accreted over the estimated life of the loans or securities using the interest method.

A transfer of financial assets in which control is surrendered is accounted for as a sale to the extent that consideration other than a beneficial interest in the transferred assets is received in the exchange. Liabilities and derivatives incurred or obtained by the transfer of financial assets are required to be measured at fair value, if practicable. Also, servicing assets and other retained interests in the transferred assets must be measured by allocating the previous carrying value between the asset sold and the interest retained, if any, based on their relative fair values at the date of transfer.

To determine the value of the securities, IFC estimates future rates of prepayments, prepayment penalties to be received by IFC, delinquencies, defaults and default loss severity and their impact on estimated cash flows. At December 31, 1999, IFC used a 4.39% constant default rate estimate with a 73.78% severity resulting in loss estimates of 2.08%. These estimates are based on historical loss data for comparable loans. IFC estimates prepayments by evaluating

historical prepayment performance of comparable mortgage loans and trends in the industry. At December 31, 1999, IFC used a constant prepayment assumption of 1.37% to estimate the prepayment characteristics of the underlying collateral. These assumptions may fluctuate depending on market conditions.

4. Securities Available-for-Sale and Securities Held-for-Trading

IFC classifies investment and mortgage-backed securities as held-to-maturity, available-for-sale, and/or trading securities. Held-to-maturity investment and mortgage-backed securities are reported at amortized cost, available-for-sale securities are reported at fair value with unrealized gains and losses, net of related income taxes, as a separate component of shareholders' equity, and trading securities are reported at fair value with unrealized gains and losses reported in operations. IFC's investment securities are held as available-for-sale, reported at fair value with unrealized gains and losses net of related income taxes reported as a separate component of shareholders' equity. Premiums or discounts obtained on investment securities are accreted or amortized to interest income over the estimated life of the investment securities using the interest method.

Residual interests in securitization of mortgage loans are recorded as a result of the sale of mortgage loans through securitizations. IFC sells a portfolio of mortgage loans to a special purpose entity that has been established for the limited purpose of buying and reselling IFC's mortgage loans. The special purpose entity then transfers the same mortgage loans to a Real Estate Mortgage Investment Conduit or owners trust (the Trust). The Trust issues interest-bearing asset-backed securities in an amount equal to the aggregate principal balance of the mortgage loans. IFC typically sells these certificates at face value and without recourse except that representations and warranties customary to the mortgage banking industry are provided by IFC. IFC may provide a credit enhancement for the benefit of the investors in the form of additional collateral (over-collateralization) held by the Trust. The over-collateralization account is required to be maintained at specified levels.

At the closing of each securitization, IFC removes from its consolidated balance sheets the loans held-for-sale and adds to its consolidated balance sheet the cash received, and the estimated fair value of the portion of the mortgage loans retained from the securitizations (Residuals). The Residuals consist of the over-collateralization account and the net interest receivables which represent the estimated cash flows to be received by the Trust in the future. The excess of the cash received and the assets retained by IFC over the carrying value of the mortgage loans sold, less transaction costs, equals the net gain on sale of mortgage loans recorded by IFC.

IFC allocates its basis in the mortgage loans between the portion of the mortgage loans sold through the certificates and the portion retained based on the relative fair values of those portions on the date of the sale. IFC may recognize gains or losses attributable to the changes in the fair value of the residuals, which are recorded at estimated fair value and accounted for as held-for-trading securities at IFC. The market for the purchase or sale of residuals is not considered liquid. IFC determines the estimated fair value of the residuals by discounting the expected cash flows using a discount rate which IFC believes is commensurate with the risks involved. At December 31, 1999, IFC used a weighted average discount rate of approximately 16.8%. Most of the residual interests generated by IFC are sold to IMH and accounted for as available-for-sale securities at IMH.

The Company receives periodic servicing fees for the servicing and collection of the mortgage loans as master servicer of the securitized loans. The Company is also entitled to the cash flows from the residual that represent collections on the mortgage loans in excess of the amounts required to pay the certificate principal and interest, the servicing fees and certain other fees such as trustee and custodial fees. At the end of each collection period, cash collected from the mortgage loans are allocated to the base servicing and other fees for the period, then to the certificate holders for interest at the pass-through rate on the certificates plus principal as defined in the servicing agreements. If the amount of cash required for the above allocations exceeds the amount collected during the collection period, the shortfall is drawn from the over-collateralization account. If the cash collected during the period exceeds the amount necessary for the above allocations, and there is no shortfall in the related over-collateralization account, the excess is

released to the Company. If the over-collateralization account balance is not at the required credit enhancement level, the excess cash collected is retained in the over-collateralization account until the specified level is achieved. The cash and collateral in the over-collateralization account is restricted from use by the Company. Pursuant to certain servicing agreements, cash held in the over-collateralization accounts may be used to make accelerated principal paydowns on the certificates to create additional excess collateral in the over-collateralization account.

5. Mortgage Loans Held-for-Sale

Mortgage loans held-for-sale are stated at the lower of cost or market in the aggregate as determined by outstanding commitments from investors or current investor yield requirements. Interest is recognized as revenue when earned according to the terms of the mortgage loans and when, in the opinion of management, it is collectible. Nonrefundable fees and direct costs associated with the origination or purchase of loans are deferred and recognized when the loans are sold as gain or loss on sale of mortgage loans. It is the policy of the Company to construct hedge positions, which will limit exposure to a rise or decline of 25 basis points in yield or approximately a one-point change in price of the benchmark instrument.

6. Premises and Equipment

Premises and equipment are stated at cost, less accumulated depreciation or amortization. Depreciation on premises and equipment is recorded using the straight-line method over the estimated useful lives of individual assets (three to seven years).

7. Mortgage Servicing Rights

The Company allocates a portion of the cost of acquiring a mortgage loan to the mortgage loan servicing rights based on its fair value relative to the components of the loan. To determine the fair value of the servicing rights created, IFC uses a valuation model that calculates the present value of future net servicing revenues to determine the fair value of the servicing rights. In using this valuation method, IFC incorporates assumptions that it believes market participants would use in estimating future net servicing, an inflation rate, ancillary income per loan, a prepayment rate, a default rate and a discount rate commensurate with the risk involved. MSRs are amortized in proportion to, and over the period of expected net servicing income.

The mortgage servicing rights are considered impaired when the fair value using a discounted cash flow analysis is less than the carrying value. In that event, an impairment loss is recognized in the respective period.

As of December 31, 1999 and 1998, IFC is the master servicer for $1.4 billion and $1.5 billion of loans collateralizing REMIC securities and $885.2 million and $1.1 billion of mortgage loans collateralizing CMOs, respectively. IFC recognizes gain or loss on the sale of servicing rights when the sales contract has been executed and ownership is determined to have passed to the purchasing party. Gains and losses are computed by deducting the basis in the servicing rights and any other costs associated with the sale from the purchase price.

8. Income Taxes

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax base. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

9. Futures

To control risk, IFC uses future contracts on Treasury Bonds and Treasury notes to hedge against interest rate fluctuations and options on futures. The use of these instruments provides for increased liquidity, lower transaction costs and more effective short-term coverage than cash and mortgage-backed securities. However, IFC is vulnerable to the basis risk that is inherent in cross-hedging transactions. IFC uses the buying and selling of futures contracts on Treasury bonds and Treasury notes when the market is vulnerable to day to day corrections. Executing hedges with these instruments allows IFC to more effectively hedge the risks of corrections or reverses in the market without committing mandatory sales on mortgage-backed securities or cash. IFC utilizes these instruments on a short-term basis to fine-tune its overall hedge position at a lower cost. The Company's policy is to defer hedging gains or losses until the related asset is sold. The hedge is then recognized and applied against the gain or loss on the sale.

10. Forward Contracts and Options

In order to hedge against a change in market value of the loans it acquires, IFC sells mortgage-backed securities through forward delivery contracts. Income or loss on these contracts is recorded at the time of sale of the related contracts or loans as a component of the gain or loss on sale of the loans. If any party to the contracts fails to completely perform, IFC would be exposed to additional interest rate risk. IFC’s principal hedging activity consists of optional and mandatory commitments to deliver closed mortgage loans to institutional investors, which do not require any collateral deposits. Written options are stated at market value.

11. Servicing Income

Servicing income is reported as earned, principally on a cash basis when the majority of the service process is completed.

12. Recent Accounting Pronouncements

In June 1998, the FASB issued SFAS 133, which establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, (collectively referred to as derivatives) and for hedging activities. It requires that an entity recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value. If certain conditions are met, a derivative may be specifically designated as (a) a hedge of the exposure to changes in the fair value of a recognized asset or liability or an unrecognized firm commitment, (b) a hedge of the exposure to variable cash flows of a forecasted transaction, or (c) a hedge of the foreign currency exposure of a net investment in a foreign operation, an unrecognized firm commitment, an available-for-sale security, or a foreign-currency-denominated forecasted transaction. This statement is effective for all fiscal quarters of fiscal years beginning after June 15, 1999. SFAS 133 was amended by SFAS No. 137, which allows deferral of SFAS 133 for all fiscal quarters of fiscal years beginning after July 15, 2000. Management is evaluating the impact of implementation of SFAS 133 on the Company’s financial position and results of operations.

Note B—Mortgage Loans Held-for-Sale

Mortgage loans purchased by IFC are fixed and adjustable-rate non-conforming mortgage loans secured by first and second liens on single-family residential properties. During the years ended December 31, 1999 and 1998, IFC acquired $1.7 billion and $2.2 billion, respectively, of mortgage loans and sold $1.8 billion and $2.6 billion, respectively, of mortgage loans. Of the mortgage loans sold by IFC during 1999 and 1998, $638.3 million and $866.7 million, respectively, were sold to IMH including premiums of $877,000 and $23.8 million, respectively. At December 31, 1999 and 1998, approximately 23% and 50%, respectively, of mortgage loans held-for-sale were collateralized by properties located in California. During 1999 and 1998, IFC acquired none and $54.4 million, respectively, of fixed-rate mortgage loans secured

by second liens on single family residential properties with loan-to-value ratios of approximately 125%, of which $193,000 of principal balance was outstanding at December 31, 1999.

Mortgage loans held for sale consisted of the following:

	At December 31,	
	1999	1998
	(in thousands)	
Mortgage loans held-for-sale	$ 66,041	$ 247,079
Premium on loans	1,251	5,226
Deferred hedging	792	263
	$ 68,084	$ 252,568

Included in other liabilities at December 31, 1999 and 1998 is an allowance for repurchases of $592,000 and $838,000, respectively.

Note C—Premises and Equipment

Premises and equipment consisted of the following:

	At December 31,	
	1999	1998
	(in thousands)	
Premises and equipment	$ 6,146	$ 3,463
Less accumulated depreciation	(2,571)	(1,485)
	$ 3,575	$ 1,978

Note D—Mortgage Servicing Rights

Activity for mortgage servicing rights was as follows:

	For the year ended December 31,	
	1999	1998
	(in thousands)	
Beginning Balance	$ 14,062	$ 15,568
Additions	7,968	8,577
Impairment of mortgage servicing rights	(1,078)	(3,722)
Amortization	(5,331)	(6,361)
Ending balance	$ 15,621	$ 14,062

At December 31, 1999 and 1998, approximately $6.2 million and $5.6 million, respectively, of mortgage servicing rights relates to $1.6 billion and $1.1 billion, respectively, of mortgage loans sold to IMH.

Note E—Other Borrowings

IFC enters into reverse repurchase agreements with major brokerage firms to fund the purchase of mortgage loans. Mortgage loans underlying reverse repurchase agreements are delivered to dealers that arrange the transactions. IFC has entered into an uncommitted warehouse line agreement to obtain financing up to $200.0 million from a major investment bank. The margins on the reverse repurchase agreements are based on the type of collateral used and generally range

from 95% to 98% of the fair market value of the collateral. The interest rates on the borrowings are indexed to LIBOR plus a spread of 85 basis points to 125 basis points depending on the type of collateral used.

The following tables sets forth information regarding reverse repurchase agreements (in thousands):

	At December 31, 1999				
	Type of Collateral	Commitment Amount	Reverse Repurchase Liability	Underlying Collateral	Maturity Date
Lender 1	Mortgages	$ 181	$ 181	$ 253	N/A
		$ 181	$ 181	$ 253	

	At December 31, 1998				
	Type of Collateral	Commitment Amount	Reverse Repurchase Liability	Underlying Collateral	Maturity Date
Lender 1	Mortgages	$ 25,024	$ 25,024	$ 30,073	N/A
Lender 2	Mortgages	42,034	42,034	43,141	N/A
		$ 67,058	$ 67,058	$ 73,214	

Note F—Income Taxes

IFC's income taxes (benefit) are as follows:

	For the year ended December 31,		
	1999	1998	1997
		(in thousands)	
Current income taxes:			
Federal	$ 248	$ (3,673)	$ 4,064
State	2	—	1,346
Total current income taxes	250	(3,673)	5,410
Deferred income taxes:			
Federal	2,115	(3,533)	433
State	862	(1,532)	293
Total deferred income taxes	2,977	(5,065)	726
Total income taxes (benefit)	$ 3,227	$ (8,738)	$ 6,136

The Company's effective income taxes (benefit) differ from the amount determined by applying the statutory Federal rate of 34% for the years ended December 31, 1999, 1998, and 1997 is as follows:

	1999	1998	1997
		(in thousands)	
Income taxes (benefit) at Federal tax rate	$ 2,570	$ (7,735)	$ 4,942
California franchise tax, net of Federal income tax (benefit)	570	(1,011)	1,082
Other	87	8	112
	$ 3,227	$ (8,738)	$ 6,136

The tax effected cumulative temporary differences that give rise to deferred tax assets and liabilities as of December 31, 1999 and 1998 are as follows:

	1999	1998
	(in thousands)	
Deferred tax assets:		
Deferred revenue	$ 3,142	$ 4,364
Forward commitments	14	368
Depreciation	28	19
Salary accruals	169	188
Other accruals	585	103
Loan mark-to-market	—	331
Non-accrual loans	91	685
Provision for repurchases	244	345
Contribution carryover	—	25
Minimum tax credit	292	263
Net operating loss	2,871	2,926
Total gross deferred tax assets	7,436	9,617
Deferred tax liabilities:		
Mortgage servicing rights	6,168	5,412
Deferred gain	449	440
Mark to market	31	—
Total gross deferred tax liabilities	6,648	5,852
Net deferred tax (asset) liability	$ (788)	$ (3,765)

As of December 31, 1999, the Company has net operating loss carry-forwards for federal and state income tax purposes of $6.8 million, which are available to offset future taxable income, if any, through 2018 and 2004, respectively. In addition, the Company has an alternative minimum tax credit carry-forward of approximately $292,000 which is available to reduce future federal regular income taxes, if any, over an indefinite period.

The Company believes that the deferred tax asset will more likely than not be realized due to the reversal of the deferred tax liability and expected future taxable income. In determining the possible future realization of deferred tax assets, future taxable income from the following sources are taken into account: (a) the reversal of taxable temporary differences, (b) future operations exclusive of reversing temporary differences and (c) tax planning strategies that, if necessary, would be implemented to accelerate taxable income into years in which net operating losses might otherwise expire.

Note G—Disclosures About Fair Value of Financial Instruments

The estimated fair value amounts have been determined by IFC using available market information and appropriate valuation methodologies, however, considerable judgment is necessarily required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented are not necessarily indicative of the amounts IFC could realize 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.

	December 31, 1999		December 31, 1998	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(in thousands)			
Assets				
Cash and cash equivalents	$ 8,805	$ 8,805	$ 422	$ 422
Securities available-for-sale	1,887	1,887	5,965	5,965
Securities available-for-trading	—	—	5,300	5,300
Mortgage loans held-for-sale	68,084	68,084	252,568	252,568
Due from affiliates	4,307	4,307	9,152	9,152
Liabilities				
Borrowings from IWLG	66,125	66,125	192,900	192,900
Other borrowings	181	181	67,058	67,058
Due to affiliates	14,500	14,500	24,382	24,382
Off-balance sheet loan commitments	—	34	—	895

	December 31, 1999		
Off-balance sheet items	Notional Amount	Carrying Value	Unrealized Gain
	(in thousands)		
Forward contracts	$ 110,000	$ —	$ 471
Futures contracts	10,000	—	54
Option contracts	20,000	95	30

The fair value estimates as of December 31, 1999 and 1998 are based on pertinent information available to management as of that date. Although management is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since those dates and, therefore, current estimates of fair value may differ significantly from the amounts presented. The fair value of off-balance sheet items for 1998 was not deemed material.

The following describes the methods and assumptions used by IFC in estimating fair values:

Cash and Cash Equivalents

Fair value approximates carrying amounts as these instruments are demand deposits and do not present unanticipated interest rate or credit concerns.

Securities Available-for-Sale and Securities Held-for-Trading

To determine the value of the securities, the Company estimates future rates of prepayments, prepayment penalties to be received by the Company, delinquencies, defaults and default loss severity and their impact on estimated cash flows.

Mortgage Loans Held-for-Sale

Fair value of mortgage loans held-for-sale is estimated based on quoted market prices from dealers and brokers for similar types of mortgage loans.

Borrowings from IWLG

Fair value approximates carrying amounts because of the short-term maturity of the liabilities.

Other Borrowings

Fair value approximates carrying amounts because of the short-term maturity of the liabilities.

Due From / To Affiliates

Fair value approximates carrying amounts because of the short-term maturity of the liabilities and does not present unanticipated interest rate or credit concerns.

Off-Balance Sheet Items

Fair value of loan commitments, including hedging positions, is determined in the aggregate based on current investor yield requirements.

Fair value of forward, futures and options contracts is based on broker quotes.

Note H—Employee Benefit Plans

Profit Sharing and 401(k) Plan

IFC does not have its own 401(k) or profit sharing plan. As such, employees of IFC participate in ICII's 401(k) plan. Under ICII's 401(k) plan, employees of the Company may contribute up to 14% of their salaries. The Company will match 50% of the first 4% of employee contributions. An additional Company contribution may be made at the discretion of IFC. The Company recorded approximately $135,000, $340,000 and $204,000 for matching and discretionary contributions during 1999, 1998 and 1997, respectively.

Note I—Related Party Transactions

Related Party Cost Allocations

In December 1999, IFC entered into a services agreement with ICAI, a subsidiary of ICII, under which ICAI provides various services to IFC, including data processing, human resource administration, general ledger accounts, check processing, remittance processing and payment of accounts payable. ICAI charges fees for each of the services based upon usage. The charge to IFC for coverage is based upon a pro rata portion of costs ICAI incurred for its various policies. Total allocation of expense for the years ended December 31, 1999, 1998 and 1997 was $180,000, $178,000 and $152,000, respectively.

During 1999 and 1998, IMH and IWLG were allocated data processing, executive and operations management, and accounting services that IFC incurred during the normal course of business per the Company's submanagement agreement with RAI Advisors Inc. (RAI). IFC, through RAI, charged IMH and IWLG for management and operating services based upon usage which management believes was reasonable. In May 1999, the submanagement agreement with RAI was terminated and IFC entered into a new submanagement agreement with FIC Management, Inc., pursuant to which IFC provides services to ICH. Prior to the submanagement agreement with RAI and after RAI was terminated, IMH and IWLG were allocated data processing, executive and operations management, and accounting services that IFC incurred during the normal course of business. IFC charged IMH and IWLG for management and operating services

based upon usage which management believes was reasonable. Total cost allocations charged by IFC to IMH and IWLG for the year ended Decemb er 31, 1999, 1998 and 1997 were $1.2 million, $968,000 and $385,000, respectively.

Lease Agreement: IMH and IFC entered into a premises operating sublease agreement (see Note J—Commitments and Contingencies) to rent approximately 74,000 square feet of office space in Newport Beach, California, for a ten-year term, which expires in May 2008. IMH and IFC pay monthly rental expenses and allocate the cost to subsidiaries and affiliated companies on the basis of square footage occupied. The majority of occupancy charges incurred were paid by IFC as most of the Company's employees are employed by the Conduit Operations. Total rental expense for the years ended December 31, 1999 and 1998 were $1.1 million and $1.3 million, of which $1.0 million and $1.2 million was paid by IFC.

Credit Arrangements – Current

IFC maintains a warehouse financing facility with IWLG. Advances under such warehouse facilities bear interest at Bank of America's prime rate. As of December 31, 1999 and 1998, amounts outstanding on IFC's warehouse line with IWLG were $66.1 million and $192.9 million, respectively. Interest expense recorded by IFC related to warehouse lines with IWLG for the years ended December 31, 1999, 1998 and 1997 was $18.4 million, $32.7 million and $33.4 million, respectively.

During the normal course of business, IFC may advance or borrow funds on a short-term basis with affiliated companies. Advances to affiliates are reflected as "Due from affiliates", while borrowings are reflected as "Due to affiliates" on IFC's balance sheet. These short-term advances and borrowings bear interest at a fixed rate of 8.00% per annum. Interest income recorded by IFC related to short-term advances due from affiliates for the years ended December 31, 1999, 1998 and 1997 was $463,000, $1.7 million and $500,000, respectively. Interest expense recorded by IFC related to short-term advances due to affiliates for the years ended December 31, 1999, 1998 and 1997 was $977,000, $2.0 million and $688,000, respectively.

Transactions with IMH and IWLG

Purchase of Mortgage Loans: During the years ended December 31, 1999 and 1998, IFC purchased from IMH mortgage loans having a principal balance of $10.8 million and $170.4 million, respectively, including premiums of $294,000 and $7.7 million, respectively.

Advances: During 1999, IFC was advanced $14.5 million in cash from IMH at an interest rate of 9.50% per annum in exchange for an interest only note due June 30, 2004, in anticipation of the initial capitalization of the Bank and to fund the operations of IFC and other strategic opportunities deemed appropriate by IFC. Interest expense recorded by IFC related to this note was $696,000.

Sale of Mortgage Loans: During the years ended December 31, 1999 and 1998, IFC sold to IMH mortgage loans having a principal balance of $637.4 million and $842.9 million, respectively. The loans were sold with premiums of $877,000 and $23.9 million, respectively. Servicing rights on all mortgages purchased by IMH were retained by IFC.

Purchases and Sales of Mortgage-Backed Securities: During the years ended December 31, 1999 and 1998, IFC sold $22.0 million and $60.6 million, respectively, of mortgage-backed securities to IMH for $18.3 million and $56.1 million, respectively, net of discounts of $3.7 million and $4.5 million, respectively. During the years ended December 31, 1999 and 1998 IFC purchased $7.5 million and none of mortgage-backed securities from IMH for $3.8 million and none, respectively, net of discounts of $3.7 million and none, respectively. IFC issued the mortgage-backed securities during 1999 and 1998 in connection with its REMIC securitizations.

Transactions with WSI

Purchase of Mortgage Loans: During the years ended December 31, 1999 and 1998, IFC acquired $5.4 million and $4.2 million of mortgage loans, respectively from WSI, an affiliate of the Company. James Walsh, Executive Vice President of WSI, is a Director of the Company.

Transactions with Impac Lending Group (ILG)

Purchase of Mortgage Loans: During the year ended December 31, 1999, IFC acquired $89.2 million of mortgage loans from Impac Lending Group, an affiliate of the Company.

Transactions with RAI

Submanagement Agreement: In 1997, IFC entered into a submanagement agreement with RAI under which IMH and IFC provided various services to ICH as RAI deems necessary, including facilities and costs associated therewith, technology, human resources, management information systems, general ledger accounts, check processing and accounts payable, plus a 15% service charge. RAI charges ICH for these services based upon usage. Total cost allocations RAI charged to ICH for the year ended December 31, 1998 were $521,000. In May 1999, the Submanagement Agreement with RAI was terminated and IFC entered into a new submanagement agreement with FIC Management, Inc. pursuant to which IFC provides service to ICH.

Non-Compete Agreement and Right of First Refusal Agreement

Pursuant to the Non-Compete Agreement executed on the date of the ICH initial public offering, IFC will not acquire any commercial mortgages for a period of the earlier of nine months from the closing of the ICH initial public offering or the date upon which ICH and/or ICCC accumulates (for investment or sale) $300.0 million of commercial mortgages or commercial mortgage-backed securities. This agreement expired in March 1998.

Pursuant to the Right of First Refusal Agreement by and among IFC, IMH, ICH, ICCC and RAI, pursuant to which, in part, RAI will agree that any mortgage loan or mortgage-backed security investment opportunity which is offered to it on behalf of either ICH, IMH any affiliated REIT will first be offered to that entity whose initial primary business as described in its initial public offering documentation most closely aligns with such investment opportunity. The Right of First Refusal Agreement was terminated in May 1999.

Note J—Commitments and Contingencies

Master Servicing

Properties securing mortgage loans in IFC's master servicing portfolio are primarily located in California. As of December 31, 1999 and 1998, approximately 40% of mortgage loans in IFC's master servicing portfolio were located in California. As of December 31, 1999 and 1998, IFC was master servicing loans totaling approximately $2.9 billion and $3.7 billion, respectively, of which $2.8 billion and $3.5 billion, respectively, were serviced for others. IFC is the master servicer for $1.4 billion and $1.5 billion, respectively of loans collateralizing fixed rate REMIC securities and $885.2 million and $1.1 billion, respectively, of loans collateralizing CMOs. Related fiduciary funds are held in trust for investors in non-interest bearing accounts. These funds are segregated in special bank accounts and are held as deposits at Southern Pacific Bank.

Master Commitments

IFC establishes mortgage loan purchase commitments (Master Commitments) with sellers that, subject to certain conditions, entitle the seller to sell and obligate IFC to purchase a specified dollar amount of non-conforming mortgage loans over a period generally ranging from six months to one year. The terms of each Master Commitment specify whether a seller may sell loans to IFC on a mandatory, best efforts or optional basis. Master commitments generally do not obligate IFC to purchase loans at a specific price, but rather provide the seller with a future outlet for the sale of its originated loans based on IFC's quoted prices at the time of purchase. As of December 31, 1999 and 1998, IFC had outstanding short term Master Commitments with 88 and 54 sellers, respectively, to purchase mortgage loans in the aggregate principal amount of $1.9 billion and $1.5 billion, respectively, over periods ranging from six months to one year, of which $747.5 million and $522.3 million, respectively, had been purchased or committed to be purchased pursuant to rate locks. These rate-locks were made pursuant to Master Commitments, bulk rate-locks and other negotiated rate-locks. There is no exposure to credit loss in this type of commitment until the loans are funded, and interest rate risk associated with the short-term commitments is mitigated by the use of forward contracts to sell loans to investors.

Following the issuance of a specific rate-lock, IFC is subject to the risk of interest rate fluctuations and enters into hedging transactions to diminish such risk. Hedging transactions may include mandatory or optional forward sales of mortgage loans or mortgage-backed securities, interest rate caps, floors and swaps, mandatory forward sales, mandatory or optional sales of futures, and other financial futures transactions. The nature and quantity of hedging transactions are determined by the management of IFC based on various factors, including market conditions and the expected volume of mortgage loan purchases. Deferred hedging gains and losses are presented on IFC's balance sheet in other assets. These deferred amounts are recognized upon the sale or securitization of the related mortgage loans. Deferred hedging gains and losses are presented on IFC's balance sheet in mortgage loans held-for-sale. As of December 31, 1999 and 1998, IFC had $792,000 and $263,000, respectively, of deferred hedging losses included in mortgage loans held-for-sale.

Forward Contracts

IFC sells mortgage-backed securities through forward delivery contracts with major dealers in such securities. At December 31, 1999 and 1998, IFC had $110.0 million and $46.0 million, respectively, in outstanding commitments to sell mortgage loans through mortgage-backed securities. These commitments allow IFC to enter into mandatory commitments when IFC notifies the investor of its intent to exercise a portion of the forward delivery contracts. IFC was not obligated under mandatory commitments to deliver loans to such investors at December 31, 1999 and 1998. The credit risk of forward contracts relates to the counterparties' ability to perform under the contract. IFC evaluates counterparties based on their ability to perform prior to entering into any agreements.

Futures Contracts

IFC sells futures contracts against five and ten-year Treasury notes with major dealers in such securities. At December 31, 1999 and 1998, IFC had $10.0 million and none, respectively, in outstanding commitments to sell Treasury notes which expire within 90 days.

Options

In order to protect against changes in the value of mortgage loans held for sale, IFC may sell call or buy put options on U.S. Treasury bonds and mortgage-backed securities. IFC generally sells call or buys put options to hedge against adverse movements of interest rates affecting the value of its mortgage loans held for sale. The risk in writing a call option is that IFC gives up the opportunity for profit if the market price of the mortgage loans increases and the option is exercised. IFC also has the additional risk of not being able to enter into a closing transaction if a liquid secondary market does not exist. The risk of buying a put option is limited to the premium IFC paid for the put option. IFC had written option contracts with an outstanding principal balance of $20.0 million and $25.0 million at December 31, 1999 and 1998,

respectively. IFC received approximately $95,000 and $134,000 in premiums on these options at December 31, 1999 and 1998, respectively.

Sales of Loans and Servicing Rights

In the ordinary course of business, IFC is exposed to liability under representations and warranties made to purchasers and insurers of mortgage loans and the purchasers of servicing rights. Under certain circumstances, IFC is required to repurchase mortgage loans if there has been a breach of representations or warranties. In the opinion of management, the potential exposure related to these representations and warranties will not have a material adverse effect. At December 31, 1999 and 1998, included in other liabilities are $592,000 and $838,000, respectively, in allowances for repurchases related to possible off-balance sheet recourse and repurchase agreement provisions.

Note K—Quarterly Financial Data (unaudited)

Selected quarterly financial data for 1999 follows (in thousands):

	For the Three Months Ended,			
	December 31,	September 30,	June 30,	March 31,
Net interest income	$ (571)	$ 392	$ 363	$ 88
Non-interest income	4,204	10,427	11,181	7,486
Non-interest expense (including income taxes)	4,873	7,771	10,121	6,473
Net earnings (loss)	(1,240)	3,048	1,423	1,101

Selected quarterly financial data for 1998 follows (in thousands):

	For the Three Months Ended,			
	December 31,	September 30,	June 30,	March 31,
Net interest income	$ 1,031	$ 1,387	$ 1,333	$ 4,016
Non-interest income	(8,469)	(9,103)	6,973	4,916
Non-interest expense (including income taxes)	2,627	224	6,491	6,755
Net earnings (loss)	(10,065)	(7,940)	1,815	2,177

Corporate Officers and Directors
Joseph R. Tomkinson
Chairman of the Board, Chief Executive Officer

William S. Ashmore
Director, President and Chief Operating Officer

Richard J. Johnson
Executive Vice President, Chief Financial Officer

Gretchen D. Verdugo
Senior Vice President, Chief Accounting Officer

Ronald Morrison
General Counsel, Corporate Secretary

James Walsh
Director
Managing Director, Sherwood Trading, Inc.

Frank P. Filipps
Director
Chairman, CEO Radian Guaranty

Stephen Peers
Director
Managing Director, Bear Stearns & Company

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Form 10 -K
A copy of the Company's annual report on Form 10-K as filed with the Securities and Exchange Commission is available to stockholders without charge by contacting the Company's investor relations department.

The matters discussed in this annual report to stockholders include forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, which can be identified by the use of forward-looking terminology such as "may", "will", "intend", "should", "expect", "anticipate", "estimate", or "continue" or the negatives thereof or other comparable terminology. The Company's actual results could differ materially from those anticipated in such forward-looking statements as a result of certain factors, including, but not limited to, economic conditions, product demand, competitive products and pricing, state and federal regulations and other risks indicated in filings with the Securities and Exchange Commission.

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