SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K/A

Amendment No. 1

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

For the fiscal year ended December 31, 2003

or

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

For the transition period from _________ to _________.

Commission File Number: 1-14100

IMPAC MORTGAGE HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

Maryland	**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	**New York Stock Exchange**
Preferred Share Purchase Rights	**New York 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 x No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of 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. ¨

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2)

Yes x No ¨

As of June 30, 2003, the aggregate market value of the voting stock held by non-affiliates of the registrant was approximately $838.5 million, based on the closing sales price of common stock on the American Stock Exchange on that date. For purposes of the calculation only, all directors and executive officers of the registrant have been deemed affiliates. There were 62,186,866 shares of common stock outstanding as of March 10, 2004.

No documents are incorporated by reference.

Table of Contents

IMPAC MORTGAGE HOLDINGS, INC.

2003 FORM 10-K/A ANNUAL REPORT

EXPLANATORY NOTE

This document includes a restatement of our consolidated financial statements. The restatements were necessary to conform with accounting principles generally accepted in the United States of America (GAAP) and reflect the following:

the correction of our revenue recognition policy with respect to the cash sale of mortgage loan servicing rights (MSRs) to unrelated third parties when the mortgage loans are retained. Previously, we recognized gains in the period in which the mortgage servicing rights were sold for the amount of cash proceeds received. We now allocate a portion of the accounting basis of the mortgage loans to the mortgage servicing rights, which results in a discount to the mortgage loans retained. That discount is accreted as an adjustment to yield on mortgage assets over the life of the related mortgage loans;

the correction of our accounting for derivative financial instruments (derivatives) and interest rate risk management activities related to the variability in expected future cash flows associated with a financing obligation or future liability (a cash flow hedge). Upon review, we now believe that the documentation of our cash flow hedge accounting relationships were deficient as to the specificity of the underlying hedged transaction in order to assess hedge effectiveness and measurement of ineffectiveness as required by the stringent applicable accounting standards. As such, we made the determination that it was not appropriate to apply cash flow hedge accounting for purposes of our GAAP financial statements. In addition, we determined that certain forward purchase commitments on mortgage loans meet the definition of a derivative and now need to be accounted for as such in the financial statements;

the reclassification of certain derivative gains and losses to mark-to-market gain (loss) derivative instruments as opposed to an adjustment to the yield on mortgage assets as a result of the elimination of cash flow hedge accounting, as stated above; and

the elimination of certain inter-company balance sheet and income statement items, principally finance receivables and the related interest income and expense, with Impac Funding Corporation, our mortgage operations, prior to its consolidation on July 1, 2003.

Although these corrections have an effect on net earnings, these corrections and reclassifications have no effect on taxable income, which is an important factor in determining the amount of dividends paid to our stockholders. In addition, beginning and ending cash and cash equivalents for all reporting periods remain unchanged.

This report on Form 10-K/A for the year ended December 31, 2003 reflects corrections and restatements of the following financial statements: (a) consolidated balance sheets as of December 31, 2003 and 2002; (b) consolidated statements of operations and comprehensive earnings for the years ended December 31, 2003, 2002 and 2001; (c) consolidated statements of changes in stockholders equity for the years ended December 31, 2003, 2002 and 2001; and (d) consolidated statements of cash flows for the years ended December 31, 2003, 2002 and 2001. For a more detailed description of the restatements and reclassifications, see Note A.2. Restatement of Consolidated Financial Statements to the accompanying notes to the consolidated financial statements and Restatement of Consolidated Financial Statements in Management s Discussion and Analysis of Financial Condition and Results of Operations contained in this report on Form 10-K/A. This report on Form 10-K/A restates certain financial information for the applicable periods set forth in Item 1. Business, Item 6. Selected Consolidated Financial Data, Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations, Item 7A. Quantitative and Qualitative Disclosures About Market Risk, Item 8. Financial Statements and Supplementary Data and Item 9A. Controls and Procedures. The financial statements, report of independent registered public accounting firm and related financial information for the affected periods contained in our prior Annual

Report on Form 10-K for the year ended December 31, 2003 should no longer be relied upon. We will not amend any other Annual Reports on Form 10-K for fiscal years prior to December 31, 2003 or Quarterly Reports on Form 10-Q for quarterly periods prior to the three months ended March 31, 2004.

Table of Contents

IMPAC MORTGAGE HOLDINGS, INC.

2003 FORM 10-K/A ANNUAL REPORT

TABLE OF CONTENTS

PART I

ITEM 1.	BUSINESS	1
	Forward-Looking Statements	1
	Available Information	1
	General Overview	1
	Long-Term Investment Operations	2
	Mortgage Operations	5
	Warehouse Lending Operations	11
	Regulation	12
	Competition	12
	Employees	13
	Revisions in Policies and Strategies	13
	Risk Factors	14
ITEM 2.	PROPERTIES	28
ITEM 3.	LEGAL PROCEEDINGS	28
ITEM 4.	SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS	29

PART II

ITEM 5.	MARKET FOR REGISTRANT S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS	30
ITEM 6.	SELECTED CONSOLIDATED FINANCIAL DATA	30
ITEM 7.	MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	33
	Restatement of Consolidated Financial Statements	33
	Consolidation of IFC	33
	Critical Accounting Policies	33
	Financial Highlights for 2003	35
	Taxable Income	35
	Results of Operations and Financial Condition	36
	Liquidity and Capital Resources	46
	Off-Balance Sheet Arrangements	50
	Contractual Obligations	50
ITEM 7A.	QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK	51
	General Overview	51

	Changes in Interest Rates	51
ITEM 8.	FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA	54
ITEM 9.	CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE	54

Table of Contents

IMPAC MORTGAGE HOLDINGS, INC.

2003 FORM 10-K/A ANNUAL REPORT

TABLE OF CONTENTS

PART II

ITEM 9A.	CONTROLS AND PROCEDURES	55

PART III

ITEM 10.	DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT	57
	Director and Executive Officer Information	57
	Audit Committee Financial Expert	59
	Section 16(a) Beneficial Ownership Reporting Compliance	59
	Code of Ethics	59
ITEM 11.	EXECUTIVE COMPENSATION	59
	Employment Agreements	61
	Compensation Committee Interlocks and Insider Participation	63
ITEM 12.	SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT	63
	Equity Compensation Plan Information	63
ITEM 13.	CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS	64
ITEM 14.	PRINCIPAL ACCOUNTANT FEES AND SERVICES	66
	Pre-Approval Policies and Procedures for Audit and Non-Audit Services	66

PART IV

ITEM 15.	EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K	67
SIGNATURES		71

Table of Contents

PART I

ITEM 1. BUSINESS

Unless the context otherwise requires, the terms Company, we, us, and our refer to Impac Mortgage Holdings, Inc. (IMH), a Maryland corporation incorporated in August 1995, and its wholly-owned subsidiaries, IMH Assets Corp., or IMH Assets, Impac Warehouse Lending Group, Inc., or IWLG, Impac Multifamily Capital Corporation, or IMCC, and Impac Funding Corporation, or IFC, together with its wholly-owned subsidiaries Impac Secured Assets Corp., or ISAC, and Novelle Financial Services, Inc., or Novelle.

Forward-Looking Statements

This report on Form 10-K/A contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements, some of which are based on various assumptions and events that are beyond our control may be identified by reference to a future period or periods or by the use of forward-looking terminology, such as may, will, believe, expect, plan, anticipate, continue, or similar terms or variations on those terms or the negative of those terms. Actua could differ materially from those set forth in forward-looking statements due to a number of factors, including, but not limited to, failure to achieve projected earnings levels, the ability to generate sufficient liquidity, the ability to access the capital markets, the size, frequency and manner of our securitizations, the ability to generate taxable income and pay dividends, risks related to restatement of our financial statements, interest rate fluctuations, frauds committed upon us, unknown weaknesses in our internal controls, natural disaster, interruption in our management information systems, new regulatory laws, increase in prepayment rates on our mortgage assets, changes in assumptions regarding estimated loan losses or fair value amounts, changes in expectations of future interest rates, the availability of financing and, if available, the terms of any financing, changes in origination and resale pricing of mortgages, changes in markets which we serve and changes in general market and economic conditions. For a discussion of these and other risks and uncertainties that could cause actual results to differ from those contained in the forward-looking statements, see Risk Factors and Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations in this report. We do not undertake, and specifically disclaim any obligation, to publicly release the results of any revisions that may be made to any forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date of such statements.

Available Information

Our Internet website address is www.impaccompanies.com. We make our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and proxy statement for our annual stockholders meetings, as well as any amendments to those reports, available free of charge through our website as soon as reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission, or SEC. You can learn more about us by reviewing our SEC filings on our website by clicking on Investor Relations located on our home page and proceeding to Financial Reports. The SEC also maintains a website at www.sec.gov that contains reports, proxy statements and other information regarding SEC registrants, including the Company.

General Overview

We are a mortgage real estate investment trust, or REIT, that is a nationwide acquirer, originator, seller and investor of non-conforming Alt-A mortgages, or Alt-A mortgages, and to a lesser extent, small-balance, multi-family mortgages, or multi-family mortgages and sub-prime, or B/C

mortgages. We also provide warehouse and repurchase financing to originators of mortgages.

We operate three core businesses:

- the long-term investment operations that is conducted by IMH, IMH Assets and IMCC;
- the mortgage operations that is conducted by IFC, ISAC and Novelle; and
- the warehouse lending operations that is conducted by IWLG.

1

Table of Contents

The long-term investment operations primarily invest in adjustable rate and fixed rate Alt-A mortgages that are acquired and originated by our mortgage operations. Alt-A mortgages are primarily first lien mortgages made to borrowers whose credit is generally within typical Fannie Mae and Freddie Mac guidelines, but have loan characteristics that make them non-conforming under those guidelines. Some of the principal differences between mortgages purchased by Fannie Mae and Freddie Mac and Alt-A mortgages are as follows:

- credit and income histories of the mortgagor;
- documentation required for approval of the mortgagor; and
- higher loan balances.

For instance, Alt-A mortgages may not have certain documentation or verifications that are required by Fannie Mae and Freddie Mac and, therefore, in making our credit decisions, we are more reliant upon the borrower s credit score and the adequacy of the underlying collateral. We believe that Alt-A mortgages provide an attractive net earnings profile by producing higher yields without commensurately higher credit losses than other types of mortgages.

The long-term investment operations also originate and invest in multi-family mortgages that are primarily hybrid adjustable rate mortgages, or hybrid ARMs, with initial fixed interest rate periods of three, five and seven years that subsequently adjust to adjustable rate mortgages. Mortgage balances generally range from $250,000 to $3.0 million. Multi-family mortgages have interest rate floors, which is the initial start rate, and prepayment penalty periods of 3, 5 and 7 years. Multi-family mortgages provide greater asset diversification on our balance sheet as borrowers of multi-family mortgages typically have higher credit scores and multi-family mortgages typically have lower loan-to-value ratios, or LTV ratios, and longer average term to payoff than Alt-A mortgages.

The long-term investment operations generate earnings primarily from net interest income earned on mortgages held for long-term investment, or long-term mortgage portfolio. The long-term mortgage portfolio consists of mortgages held as CMO collateral and mortgages held for investment on our balance sheet. Investments in Alt-A mortgages and multi-family mortgages are initially financed with short-term borrowings under reverse repurchase agreements which are subsequently converted to long-term financing in the form of collateralized mortgage obligations, or CMO, financing. Cash flow from the long-term mortgage portfolio and proceeds from the sale of capital stock also finance new Alt-A and multi-family mortgages.

The mortgage operations acquire, originate, sell and securitize primarily adjustable rate and fixed rate Alt-A mortgages and, to a lesser extent, B/C mortgages. The mortgage operations generate income by securitizing and selling mortgages to permanent investors, including the long-term investment operations. This business also earns revenue from fees associated with mortgage servicing rights, master servicing agreements and interest income earned on mortgages held for sale. The mortgage operations use warehouse facilities provided by the warehouse lending operations to finance the acquisition and origination of mortgages.

The warehouse lending operations provide short-term financing to mortgage loan originators, including the mortgage operations, by funding mortgages from their closing date until sale to pre-approved investors. This business earns fees from warehouse transactions as well as net interest income from the difference between its cost of borrowings and the interest earned on warehouse advances.

Our goal is to generate consistent reliable taxable income for distribution as dividends to our stockholders primarily from earnings generated by our core operating businesses.

Long-Term Investment Operations

The long-term investment operations invest primarily in Alt-A mortgages and, to a lesser extent, multi-family mortgages and generate revenue primarily from net interest income on its long-term mortgage portfolio. Net interest income represents the difference between income received on mortgages and the corresponding cost of financing and amortization of acquisition premiums. The mortgage operations supports the investment objectives of the long-term investment operations by supplying mortgages at prices that are comparable to those available through mortgage bankers and brokers and other third parties. We believe that retaining mortgages acquired and originated by our mortgage operations gives us a competitive advantage because of our historical understanding of the underlying credit

Table of Contents

of these mortgages and the extensive information on the performance and prepayment patterns of these types of mortgages. We also believe that Alt-A mortgages provide an attractive net earnings profile by producing higher yields without commensurately higher credit risks than other types of mortgages.

The long-term investment operations also invest in Alt-A mortgages that are acquired on a bulk basis by the mortgage operations and are underwritten to guidelines substantially similar, but not specific, to those of the mortgage operations, or non-Impac Alt-A mortgages. Historically, borrowers of non-Impac Alt-A mortgages have higher credit scores than Alt-A mortgages acquired from the mortgage operations network of correspondent sellers that are underwritten to the mortgage operations specific underwriting guidelines, or Impac Alt-A mortgages.

Long-Term Mortgage Portfolio

Alt-A mortgages that we retain for long-term investment are primarily adjustable rate mortgages, or ARMs, hybrid ARMs and, to a lesser extent, fixed rate mortgages, or FRMs. The interest rate on ARMs are typically tied to an index, such as the six-month London Interbank Offered Rate, or LIBOR, plus a spread and adjust periodically, subject to lifetime interest rate caps and periodic interest rate and payment caps. The initial interest rates on ARMs are typically lower than average comparable FRMs but may be higher than average comparable FRMs over the life of the mortgage. Hybrid ARMs are mortgages with maturity periods ranging from 15 to 30 years with initial fixed interest rate periods generally ranging from two to seven years, which subsequently adjust to ARMs. The majority of mortgages retained by the long-term investment operations have prepayment penalty features with prepayment penalty periods ranging from two to seven years. Prepayment penalties may be assessed to the borrower if the borrower refinances or, in some cases, sells the home.

During 2003, the long-term investment operations retained $5.8 billion in principal balance of primarily adjustable rate Alt-A mortgages for long-term investment which were initially acquired and originated by the mortgage operations. In addition, the long-term investment operations originated $290.5 million of multi-family mortgages. The retention and origination of Alt-A and multi-family mortgages increased the long-term mortgage portfolio to $9.3 billion at year-end 2003.

The following table presents selected information on mortgages held as CMO collateral, which comprise a substantial portion of the long-term mortgage portfolio, for the periods indicated:

	As of December 31,		
	2003	2002	2001
Percent Alt-A mortgages	99	99	95
Percent ARMs	86	85	87
Percent FRMs	14	15	13
Percent hybrid ARMs	48	35	68
Weighted average coupon	5.56	6.57	7.92
Weighted average margin	3.10	3.01	3.42
Weighted average original LTV ratio	79	82	83
Weighted average original credit score	694	683	678
Percent with active prepayment penalty	81	76	54
Prior 12-month prepayment rate	28	25	34
Lifetime prepayment rate	21	33	34

Percent of mortgages in California	64	63	63
Percent purchase transactions	57	62	70
Percent owner occupied	87	93	94
Percent first lien	99	99	99

Table of Contents

The following table presents mortgages retained and originated by the long-term investment operations by loan characteristic for the periods indicated (dollars in thousands):

	For the year ended December 31,					
	2003		2002		2001	
	Principal Balance	%	Principal Balance	%	Principal Balance	%
Mortgages by Type:						
Fixed rate first trust deeds	$ 706,227	12	$ 599,566	15	$ 17,028	1
Fixed rate second trust deeds	6,744	0	311	0	259	0
Adjustable rate first trust deeds:						
Six-month LIBOR ARMs	1,670,720	27	2,352,863	60	374,113	25
Six-month LIBOR hybrid ARMs	3,694,687	61	964,316	25	1,094,943	74
Total adjustable rate first trust deeds	5,365,407	88	3,317,179	85	1,469,056	99
Total mortgages retained	$ 6,078,378	100	$ 3,917,056	100	$ 1,486,343	100
Mortgages by Credit Quality:						
Alt-A mortgages	$ 5,760,779	95	$ 3,875,903	99	$ 1,475,269	99
Multi-family mortgages	290,527	5	25,799	1		0
B/C mortgages	27,072	0	15,354	0	11,074	1
Total mortgages retained	$ 6,078,378	100	$ 3,917,056	100	$ 1,486,343	100
Mortgages by Purpose:						
Purchase	$ 3,408,584	56	$ 2,353,727	60	$ 997,350	67
Refinance	2,669,794	44	1,563,329	40	488,993	33
Total mortgages retained	$ 6,078,378	100	$ 3,917,056	100	$ 1,486,343	100
Mortgages by Prepayment Penalty:						
With prepayment penalty	$ 4,823,027	79	$ 3,100,540	79	$ 876,798	59
Without prepayment penalty	1,255,351	21	816,516	21	609,545	41
Total mortgages retained	$ 6,078,378	100	$ 3,917,056	100	$ 1,486,343	100

For additional information regarding the long-term mortgage portfolio refer to Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations, Note C CMO Collateral, and Note D Mortgages Held for Investment in the accompanying notes to the consolidated financial statements.

Financing

We primarily finance our long-term mortgage portfolio as follows:

- issuance of CMOs;
- short-term borrowings under reverse repurchase agreements, prior to securitization as CMOs; and
- proceeds from the sale of capital stock.

As we accumulate mortgages we may issue CMOs secured by such mortgages as a means of financing. The decision to issue CMOs is based on our current and future investment needs, market conditions and other factors. Each issue of CMOs is fully payable from the principal and interest payments on the underlying mortgages securing such debt and any cash or other collateral pledged as a condition of receiving the desired rating on the debt. We earn a net interest spread on interest income on mortgages held as CMO collateral less interest and other expenses associated with CMO financing. Net interest spreads may be directly impacted by levels of early prepayment of underlying mortgages and, to the extent each CMO class has variable rates of interest, may be affected by changes in short-term interest rates. Our CMOs typically are structured as adjustable rate securities that are indexed to one-month LIBOR and fixed rate securities with interest payable monthly.

Table of Contents

When we issue CMOs for financing purposes, we seek an investment grade rating for our CMOs by nationally recognized rating agencies. To secure such ratings, 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 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 our capacity to raise additional funds through short-term secured borrowings or additional CMOs, and diminishes the potential expansion of our long-term mortgage portfolio. As a result, our objective is to pledge additional collateral for CMOs only in the amount required to obtain an investment grade rating by nationally recognized rating agencies. Our total loss exposure is limited to total capital invested in the CMOs at any point in time.

For additional information regarding CMOs refer to Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Note H CMO Borrowings in the accompanying notes to the consolidated financial statements.

Prior to the issuance of CMOs, we use reverse repurchase agreements as short-term financing at interest rates that are consistent with our investment objectives. A reverse repurchase agreement acts as a financing vehicle under which we effectively pledge our mortgages 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 maturity of the reverse repurchase agreement, we are required to repay the loan and correspondingly we receive our collateral. Our borrowing agreements require us to pledge cash, additional mortgages or additional investment securities backed by mortgages in the event the market value of existing collateral declines. We may be required to sell assets to reduce our borrowings to the extent that cash reserves are insufficient to cover such deficiencies in collateral.

For additional information regarding reverse repurchase agreements refer to Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Note G Reverse Repurchase Agreements in the accompanying notes to the consolidated financial statements.

Interest Rate Risk Management

Our primary objective is to manage exposure to the variability in future cash flows attributable to the variability of one-month LIBOR, which is the underlying index of our adjustable rate CMO borrowings. We also monitor on an ongoing basis the prepayment risks that arise in fluctuating interest rate environments. Our interest rate risk management program is formulated with the intent to offset the potential adverse effects of changing interest rates on cash flows on adjustable rate CMO borrowings.

To mitigate our exposure to the effect of changing interest rates on cash flows on our adjustable rate CMO borrowings, we acquire derivatives in the form of interest rate swaps, or swaps, interest rate cap agreements, or caps and interest rate floor agreements, or floors, collectively, derivatives. For additional information regarding interest rate risk management activities refer to Item 7A. Quantitative and Qualitative Disclosures About Market Risk and Note O Derivative Instruments in the accompanying notes to the consolidated financial statements.

Mortgage Operations

The mortgage operations acquire, originate, sell and securitize primarily adjustable rate and fixed rate Alt-A mortgages and, to a lesser extent B/C mortgages, from correspondents, mortgage bankers and brokers and retail customers.

Correspondent Acquisition Channel. The mortgage operations acquire primarily adjustable rate and fixed rate Alt-A mortgages from its network of third party correspondents on a flow (loan-by-loan) basis or on a bulk basis from correspondent mortgage companies. Correspondents originate and close mortgages under the mortgage operations mortgage programs. Correspondents include savings and loan associations, commercial banks and mortgage bankers. The mortgage operations acts as an intermediary between the originators of mortgages that may not meet the guidelines for purchase by Fannie Mae and Freddie Mac and permanent investors in mortgage-backed securities secured by or representing an ownership interest in such mortgages.

Bulk Acquisition Channel. The mortgage operations also invest in non-Impac Alt-A mortgages that are underwritten to guidelines substantially similar, but not specific, to those of the mortgage operations. These mortgages are purchased on a bulk basis and borrowers have historically had higher credit scores than Alt-A mortgages acquired from the mortgage operations network of approved correspondent sellers.

Wholesale and Retail Origination Channel. The mortgage operations market, underwrite, process and fund mortgages for wholesale and, to a lesser extent, retail customers. The wholesale origination channel works directly with mortgage bankers and brokers to originate, underwrite and fund their mortgages. Many wholesale customers cannot conduct business with the mortgage operations as correspondents because they do not have the necessary financing to close mortgages in their name. Through its retail channel, the mortgage operations markets mortgages directly to the public.

B/C Origination Channel. Novelle originates B/C mortgages through a network of wholesale mortgage bankers and brokers and sells its mortgages to third party investors for cash gains.

Marketing Strategy

We believe that we can compete effectively with other Alt-A mortgage conduits through our efficient loan purchasing process, flexible purchase commitment options, competitive pricing and by designing Alt-A mortgages that suit the needs of our correspondents and mortgage bankers and brokers and their borrowers. Our principle strategy is to expand our market position as a low-cost nationwide acquirer and originator of Alt-A mortgages, while continuing to emphasize an efficient centralized operating structure. To help accomplish this, we have developed a second-generation web-based automated underwriting and pricing system called Impac Direct Access System for Lending, or iDASLg2. iDASLg2 substantially increases efficiencies for our customers and our mortgage operations by significantly decreasing the processing time for a mortgage while improving employee productivity and maintaining superior customer service.

iDASLg2 is an interactive Internet-based system that allows our customers to automatically underwrite mortgages, enabling our customers to pre-qualify borrowers for various mortgage programs and receive automated approval decisions. iDASLg2 is intended to increase efficiencies not only for our customers but also for the mortgage operations by significantly decreasing the processing time for a mortgage. iDASLg2 improves employee production and maintains superior customer service, which together leads to higher closing ratios, improved profit margins and increased profitability at all levels of our business operations. Most importantly, iDASLg2 allows us to move closer to our correspondents and mortgage bankers and brokers with minimal future capital investment while maintaining centralization, a key factor in the success of our operating strategy. All of our correspondents submit mortgages via iDASLg2 and all wholesale mortgages delivered by mortgage bankers and brokers are directly underwritten through iDASLg2. Non-Impac mortgages purchased on a bulk basis are not underwritten through iDASLg2.

We also focus on expansion opportunities to attract correspondent originators and mortgage bankers and brokers to our nationwide network in order to increase mortgage acquisitions and originations in a controlled manner. This allows us to shift the high fixed costs of interfacing with the homeowner to our correspondents and mortgage bankers and brokers. This marketing strategy is designed to accomplish the following three objectives:

- attract a geographically diverse group of both large and small correspondent originators and mortgage bankers and brokers;
- establish relationships with correspondents and mortgage bankers and brokers that facilitate their ability to offer a variety of loan products designed by the mortgage operations; and

purchase mortgages and securitize and sell them in the secondary market or to the long-term investment operations.

In order to accomplish our production objectives, we design and offer mortgage products that we believe are attractive to potential Alt-A borrowers and to end-investors in Alt-A mortgages and mortgage-backed securities. We have historically emphasized and continue to emphasize flexibility in our mortgage product mix as part of our strategy to attract and establish long-term relationships with our correspondents and mortgage bankers and brokers. We also maintain relationships with numerous investors so that we may develop mortgage products that may be of interest to them as market conditions change. In response to the needs of our correspondents, and as part of our strategy to

facilitate the sale of our mortgages through the mortgage operations, our marketing strategy offers efficient response time in the purchase process, direct and frequent contact with our correspondents and mortgage bankers and brokers through a trained sales force and flexible commitment programs. Finally, due to the price sensitivity of most homebuyers, we are competitive in pricing our products in order to attract sufficient numbers of mortgages.

Mortgage Acquisitions and Originations

Mortgages acquired and originated by the mortgage operations are adjustable rate and fixed rate Alt-A mortgages. A portion of Alt-A mortgages that are acquired and originated by the mortgage operations exceed the maximum principal balance for a conforming loan purchased by Fannie Mae or Freddie Mac, which is currently $333,700. Mortgages that exceed such maximum principal balance are referred to as jumbo loans. We generally do not acquire or originate Alt-A mortgages with principal balances above $1.0 million. Alt-A mortgages generally consist of jumbo loans or other mortgages that are acquired and originated in accordance with underwriting or product guidelines that differ from those applied by Fannie Mae and Freddie Mac. Alt-A mortgages may involve greater risk as a result of different underwriting and product guidelines. Additionally, a portion of mortgages acquired and originated through the mortgage operations are B/C mortgages, which may entail greater credit risks than Alt-A mortgages. B/C mortgage acquisitions and originations represented 5% and 7% of total acquisitions and originations during 2003 and 2002, respectively.

We generally do not originate B/C mortgages with principal balances above $650,000. In general, B/C mortgages are residential mortgages made to borrowers with lower credit ratings than borrowers of Alt-A mortgages. B/C mortgages are normally subject to higher rates of loss and delinquency than Alt-A mortgages acquired and originated by the mortgage operations. As a result, B/C mortgages normally bear a higher rate of interest and are typically subject to higher fees than Alt-A mortgages. 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 mortgages than in underwriting Alt-A mortgages. In addition, B/C mortgages are generally subject to lower LTV ratios than Alt-A mortgages.

Mortgages acquired or originated by the mortgage operations are generally secured by first liens and, to a lesser extent, second liens on single-family residential properties with either adjustable rate or fixed interest rates. FRMs have a constant interest rate over the life of the loan, which is generally 15 or 30 years. The interest rates on ARMs are typically tied to an index, such as six-month LIBOR, plus a spread and adjust periodically, subject to lifetime interest rate caps and periodic interest rate and payment caps. The initial interest rates on ARMs are typically lower than the average comparable FRM but may be higher than average comparable FRMs over the life of the loan.

We acquire and originate mortgages with the following most common loan characteristics, although we may purchase mortgages with other interest rate, prepayment and maturity characteristics:

- FRMs that have original terms to maturity ranging from 15 to 30 years with one- to five-year prepayment penalty periods;
- ARMs that adjust based on six-month LIBOR with terms to maturity ranging from 15 to 30 years with one- to five-year prepayment penalty periods;
- two-, three- and five-year hybrid ARMs with terms to maturity ranging from 15 to 30 years that subsequently adjust to six-month LIBOR ARMs with one- to five-year prepayment penalty periods; and

adjustable rate and fixed rate interest-only mortgages with 5 to 10 year interest-only periods and terms to maturity of 30 years with one- to five-year prepayment penalty periods.

Table of Contents

The following table presents mortgage acquisitions and originations by loan characteristic for the periods indicated (in thousands):

	For the year ended December 31,					
	2003		2002		2001	
	Principal Balance	%	Principal Balance	%	Principal Balance	%
Mortgages by Type:						
Fixed rate first trust deeds	$ 3,812,952	40	$ 2,159,696	36	$ 1,570,225	50
Fixed rate second trust deeds	181,173	2	82,145	2	43,074	1
Adjustable rate first trust deeds:						
Six-month LIBOR ARMs	1,611,392	17	2,426,865	41	407,599	13
Six-month LIBOR hybrids	3,919,604	41	1,276,792	21	1,133,730	36
Total adjustable rate first trust deeds	5,530,996	58	3,703,657	62	1,541,329	49
Total mortgage acquisitions and originations	$ 9,525,121	100	$ 5,945,498	100	$ 3,154,628	100
Mortgages by Channel:						
Correspondent acquisitions:						
Impac Alt-A mortgages	$ 5,399,428	57	$ 4,286,905	72	$ 2,213,736	70
Non-Impac Alt-A mortgages	2,159,116	23	164,636	3	169,282	5
Total correspondent acquisitions	7,558,544	80	4,451,541	75	2,383,018	75
Wholesale and retail originations	1,468,697	15	1,089,008	18	683,060	22
B/C originations.	497,880	5	404,949	7	88,550	3
Total mortgage acquisitions and originations	$ 9,525,121	100	$ 5,945,498	100	$ 3,154,628	100
Mortgages by Credit Quality:						
Alt-A mortgages	$ 8,988,018	94	$ 5,515,573	93	$ 3,046,532	97
B/C mortgages (1)	537,103	6	429,925	7	108,096	3
Total mortgage acquisitions and originations	$ 9,525,121	100	$ 5,945,498	100	$ 3,154,628	100
Mortgages by Purpose:						
Purchase	$ 4,683,202	49	$ 3,288,566	55	$ 1,938,715	61
Refinance	4,841,919	51	2,656,932	45	1,215,913	39
Total mortgage acquisitions and originations	$ 9,525,121	100	$ 5,945,498	100	$ 3,154,628	100
Mortgages by Prepayment Penalty:						
With prepayment penalty	$ 7,165,949	75	$ 4,677,078	79	$ 2,058,746	65
Without prepayment penalty	2,359,172	25	1,268,420	21	1,095,882	35
Total mortgage acquisitions and originations	$ 9,525,121	100	$ 5,945,498	100	$ 3,154,628	100

(1) 2003, 2002 and 2001 includes $497.9 million, $404.9 million and $88.6 million, respectively, of B/C mortgages originated by Novelle that were subsequently sold to third party investors for cash gains.

Our mortgage acquisition and origination activities focus on those regions of the country where higher volumes of Alt-A mortgages are originated including California, Florida, New York, Colorado, New Jersey, Maryland, Virginia, Illinois, Arizona and Nevada. During the years ended December 31, 2003 and 2002, mortgages secured by California and Florida properties accounted for an aggregate of approximately 76% and 56%, respectively, of mortgage acquisitions and originations during both years.

Of the $9.5 billion in principal balance of mortgages acquired and originated in 2003, $3.7 billion, or 39%, were acquired from our top ten correspondents. Express Lending Group accounted for $925.9 million, or 10%, of mortgages acquired and originated by the mortgage operations in 2003. No other correspondents or bankers and brokers accounted for more than 10% of the total mortgages acquired and originated by the mortgage operations in 2003.

Table of Contents

Underwriting

We have developed comprehensive purchase guidelines for the acquisition and origination of mortgages. Each mortgage underwritten assesses the borrower s credit score, ability and willingness to repay the mortgage obligation and the adequacy of the mortgaged property as collateral for the mortgage. Subject to certain exceptions and the type of mortgage product, each purchased mortgage generally conforms to the loan parameters and eligibility requirements specified in our seller/servicer guide with respect to, among other things, loan amount, type of property, compliance, LTV ratio, mortgage insurance, credit history, debt service-to-income ratio, appraisal and loan documentation.

All mortgages acquired or originated under our loan programs are underwritten either by our employees or by contracted mortgage insurance companies or delegated sellers. Under all of our 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 may be validated by an enhanced desk or field review, depending on the loan program. Lending decisions are based on a risk analysis assessment after the review of the entire mortgage file. Each mortgage is individually underwritten with emphasis placed on the overall quality of the mortgage.

Seller Eligibility Requirements

Mortgages acquired by the mortgage operations are originated by various sellers, including mortgage bankers, savings and loan associations and commercial banks. Sellers are required to meet certain regulatory, financial, insurance and performance requirements established by us before they are eligible to participate in our mortgage purchase programs. Sellers must also submit to periodic reviews to ensure continued compliance with these requirements. Our current criteria for seller participation generally includes a minimum tangible net worth requirement of $500,000, approval as a Fannie Mae or Freddie Mac seller/servicer in good standing, a Housing and Urban Development, or HUD, approved mortgagee in good standing or a financial institution that is insured by the Federal Deposit Insurance Corporation, or 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 mortgage origination quality control procedures. In connection with its qualification, each seller enters into an agreement that generally provides for recourse by us against the seller in the event of a breach of representations or warranties made by the seller with respect to mortgages sold to us, which includes but is not limited to any fraud or misrepresentation during the mortgage loan origination process or upon early payment default on mortgages.

Securitization and Sale

After acquiring mortgages from correspondents on a flow or bulk basis and originating mortgages through wholesale and retail channels, the mortgage operations sell and securitize mortgages to permanent investors. The mortgage operations sell substantially all of its ARM acquisitions to the long-term investment operations at prices comparable to prices available from third party investors at the date of sale. When a sufficient volume of FRMs with similar characteristics has been accumulated, generally $100 million to $350 million, the mortgage operations may sell bulk packages, referred to as whole loan sales, to third party investors, securitize them through the issuance of mortgage-backed securities in the form of real estate mortgage investment conduits, or REMICs, or sell them to the long-term investment operations.

During 2003, the mortgage operations transferred $5.8 billion in principal balance of mortgages to the long-term investment operations, sold $2.7 billion in principal balance of mortgages as whole loan sales and sold $887.5 million in principal balance of mortgages as REMICs. Generally, the mortgage operations sells all of its mortgage acquisitions and originations to third party investors as servicing released, which means that it does not retain primary mortgage servicing rights. However, the mortgage operations does retain rights as master servicer for its securitizations, see Master Servicing below.

The period of time between when we commit to purchase mortgages and the time we sell or securitize mortgages generally ranges from 15 to 45 days, depending on certain factors, including the length of the purchase commitment

Table of Contents

period, volume by product type and the securitization process. REMICs are accounted for as sales transactions and eliminate any long-term residual investment in such mortgages. 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. REMICs created by us are structured so that one or more of the classes of securities are rated investment grade by at least one nationally recognized rating agency. The ratings for our REMICs are based upon the perceived credit risk by the applicable rating agency of the underlying mortgages, 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 mortgages as required by law or a bankruptcy court.

Master Servicing

We retain master servicing rights on substantially all of our Alt-A and multi-family mortgage acquisitions and originations. Our function as master servicer includes collecting loan payments from other loan servicers 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, we monitor compliance with our servicing guidelines and are required to perform, or to contract with a third party to perform, all obligations not adequately performed by any loan servicer. We may also be required to advance funds to cover interest payments not received from borrower s depending on the status of their mortgages. We also earn income or incur expense on principal and interest payments we receive from our borrowers until those payments are remitted to the investors in those mortgages. Master servicing fees are generally 0.03% per annum on the declining principal balances of the loans serviced. At year-end 2003, we master serviced 65,255 mortgages with a principal balance of $13.9 billion.

The following table presents the amount of delinquent mortgages in our master servicing portfolio for the periods indicated (dollars in thousands):

	As of December 31,					
	2003		2002		2001	
	Principal Balance of Mortgages	% of Master Servicing Portfolio	Principal Balance of Mortgages	% of Master Servicing Portfolio	Principal Balance of Mortgages	% of Master Servicing Portfolio
Loans delinquent for:						
60-89 days	$ 105,455	0.76%	$ 100,878	1.16%	$ 72,460	1.30%
90 days and over	87,297	0.63	71,466	0.82	72,544	1.30
Total 60 days and over	192,752	1.39	172,344	1.98	145,004	2.60
Foreclosures pending	158,261	1.14	212,309	2.44	132,571	2.38
Bankruptcies pending	19,912	0.14	26,402	0.30	22,054	0.40
Total	$ 370,925	2.67%	$ 411,055	4.72%	$ 299,629	5.38%

Servicing

We sell or subcontract all of our servicing obligations to independent third parties pursuant to sub-servicing agreements. We believe that the sale of servicing rights or the selection of third-party sub-servicers is more effective than establishing a servicing department within our mortgage operations. However, part of our responsibility is to continually monitor the performance of servicers or sub-servicers through performance reviews and regular site visits. Depending on our reviews, we may in the future rely on our internal default management group to take an ever more active role to assist servicers or sub-servicers in the servicing of our mortgages. 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 un-remedied defaults in accordance with our guidelines. Servicing fees range from 0.25% per annum for FRMs to 0.50% per annum for B/C mortgages and 0.375% for ARMs on the declining principal balances of loans serviced. We generally acquire all of our mortgages on a servicing released basis. To the extent the mortgage operations finances the acquisition of

mortgages with warehouse facilities provided by the warehouse lending operations, the mortgage operations pledges mortgages and the related servicing rights to the warehouse lending operations as collateral. As a result, the warehouse lending operations has an absolute right to control the servicing of such mortgages, including the right to collect payments on the underlying mortgages, and to foreclose upon the underlying real property in the case of default. Typically, the warehouse lending operations delegates its right to service the mortgages securing the warehouse line to the mortgage operations. The following table presents information regarding our mortgage servicing portfolio, including mortgages held-for-sale and mortgages held for long-term investment, for the periods shown (dollars in millions, except average loan size):

	As of December 31,		
	2003	**2002**	**2001**
Beginning servicing portfolio	$ 2,653.4	$ 1,754.4	$ 2,428.9
Add: Loan acquisitions and originations	9,525.1	5,945.5	3,154.7
Less: Servicing transferred and principal repayment (1)	(10,776.4)	(5,046.5)	(3,829.2)
Ending servicing portfolio	$ 1,402.1	$ 2,653.4	$ 1,754.4
Number of loans serviced	6,695	15,987	14,570
Average loan size	$ 209,000	$ 166,000	$ 120,000
Weighted average coupon	6.28%	7.26%	8.80%

(1) Includes the sale of mortgages on a servicing released basis and the sale of servicing rights on mortgages owned and scheduled and unscheduled principal repayments.

Interest Rate Risk Management

The mortgage operations manages interest rate risk and price volatility on its pipeline of rate-locked mortgage loans, or mortgage pipeline, during the time it commits to acquire or originate mortgages at a pre-determined rate and the time it purchases or funds these mortgage loans. To mitigate interest rate and price volatility risks, the mortgage operations may enter into derivatives. The nature and quantity of derivatives are determined based on various factors, including market conditions and the expected volume of mortgage acquisitions and originations. On March 9, 2004, the SEC issued Staff Accounting Bulletin No. 105, Application of Accounting Principles to Loan Commitments, or SAB 105, which clarifies the SEC s position on the accounting and valuation for commitments to originate mortgage loans held-for-sale. Consistent with SFAS 149, SAB 105 states that loan commitments are treated as derivatives. SAB 105 requires that in valuing these loan commitments entities not include cash flows associated with servicing as to do so would result in the recognition of servicing assets prior to the sale or securitization of funded loans. This valuation methodology limits a company s ability to record an asset for its mortgage pipeline as of the applicable reporting date. Prior to the issuance of SAB 105, each reporting period the mortgage operations recorded the fair value of its mortgage pipeline, inclusive of changes in benchmark interest rates and acquisition premiums. Subsequent to SAB 105, as of April 1, 2004 we record the fair value change of the mortgage pipeline based solely on interest rate fluctuations from the date of rate-lock to the applicable reporting date. For additional information regarding interest rate risk management activities refer to Item 7A. Quantitative and Qualitative Disclosures About Market Risk and Note O Derivative Instruments in the accompanying notes to the consolidated financial statements.

Warehouse Lending Operations

The warehouse lending operations provide warehouse financing to affiliated companies and reverse repurchase financing to approved non-affiliated mortgage bankers, or non-affiliated clients, some of which are correspondents of the mortgage operations, to finance mortgages during the time from the closing of the mortgages to sale or other settlement with pre-approved investors. The warehouse lending operations

relies mainly on the sale or liquidation of the mortgages as a source of repayment. Any claim of the warehouse lending operations as a secured lender in a bankruptcy proceeding may be subject to adjustment and delay. Borrowings under warehouse facilities are presented on our balance sheet as finance receivables. Terms of non-affiliated clients warehouse lines, including the commitment amount, are determined based upon the financial strength, historical performance and other qualifications of the

borrower. As of December 31, 2003, the warehouse lending operations had approved warehouse lines to non-affiliated clients of $1.0 billion, of which $630.0 million was outstanding, as compared to $665.0 million and $664.0 million, respectively, as of December 31, 2002.

Regulation

We establish underwriting guidelines that include provisions for inspections and appraisals, require credit reports on prospective borrowers and determine maximum loan amounts. Our mortgage acquisition and origination activities are subject to, among other laws, the Equal Credit Opportunity Act, Federal Truth-in-Lending Act, Real Estate Settlement Procedures Act and Home Mortgage Disclosure Act and the regulations promulgated thereunder. These laws and regulations prohibit discrimination and require the disclosure of certain basic information to mortgagors concerning credit terms and settlement costs, limit payment for settlement services to the reasonable value of the services rendered and require the maintenance and disclosure of information regarding the disposition of mortgage applications based on race, gender, geographical distribution and income level. Our mortgage acquisition and origination activities are also subject to state and local laws and regulations, including predatory lending laws, and may also be subject to applicable state usury statutes. IFC is an approved Fannie Mae and Freddie Mac seller and/or servicer. In addition, IFC is required annually to submit to Fannie Mae and Freddie Mac audited financial statements, or the equivalent, and each regulatory entity has its own financial requirements for sellers/servicers. IFC s affairs are also subject to examination by Fannie Mae and Freddie Mac at any time to assure compliance with applicable regulations, policies and procedures.

Competition

In acquiring and originating Alt-A mortgages and issuing securities backed by such loans, we compete with established mortgage conduit programs, investment banking firms, savings and loan associations, banks, thrift and loan associations, finance companies, mortgage bankers and brokers, insurance companies, other lenders and other entities purchasing mortgage assets. Consolidation in the mortgage banking industry may also reduce the number of current correspondents and independent mortgage bankers and brokers available to the mortgage operations, reducing our potential customer base and resulting in the mortgage operations acquiring and originating a larger percentage of mortgages from a smaller number of customers. Changes of this nature could negatively impact our businesses.

Mortgage-backed securities issued by the mortgage operations and the long-term investment operations face competition from other investment opportunities available to prospective investors. We face competition in our mortgage operations and warehouse lending operations from other financial institutions, including but not limited to banks and investment banks. Our main competitors include Countrywide Home Loans, IndyMac Bancorp, Inc., Greenpoint Financial Corporation, Residential Funding Corporation, Aurora Loan Services, Inc., Credit Suisse First Boston Corporation and Bear Stearns and Company, Inc.

Competition can take place on various levels, including convenience in obtaining a mortgage, service, marketing, origination channels and pricing. We depend primarily on correspondents and independent mortgage bankers and brokers for the acquisition and origination of mortgages. These independent mortgage bankers and brokers deal with multiple lenders for each prospective borrower. We compete with these lenders for the independent bankers and brokers business on the basis of price, service, loan fees, costs and other factors. Our competitors also seek to establish relationships with such bankers and brokers, who are not obligated by contract or otherwise to do business with us. Many of the institutions with which we compete in our mortgage operations and warehouse lending operations have significantly greater financial resources than we have. However, we can compete effectively with other Alt-A mortgage conduits through our efficient loan purchasing process, flexible purchase commitment options and competitive pricing and by designing Alt-A mortgages that suit the needs of our correspondents and their borrowers, which is intended to provide sufficient credit quality to our investors.

Risk factors, as outlined below, provide additional information related to risks associated with competition in the mortgage banking industry.

Table of Contents

Employees

As of December 31, 2003, we had a total of 529 full- and part-time employees and temporary and contract employees. The mortgage operations employed 480 full- and part-time employees and temporary and contract employees, of which 87 were employed by Novelle. The warehouse lending operations employed 31 full- and part-time employees and temporary and contract employees. The long-term investment operations employed 18 full- and part-time employees and temporary and contract employees. Management believes that relations with its employees are good. We are not a party to any collective bargaining agreements.

Revisions in Policies and Strategies

Our board of directors has approved our investment and operating policies and strategies. Our core operations involve the acquisition and origination of mortgages and their subsequent securitization and sale. We also act as a warehouse lender providing financing facilities to mortgage originators. These operations and their associated policies and strategies, are further described herein. Our board of directors has delegated asset/liability management to the Asset/Liability Committee, or ALCO, which reports to the board of directors at least quarterly. See a further discussion of ALCO in Item 7. Management s Discussion of Financial Condition and Results of Operations and Item 7A. Quantitative and Qualitative Disclosures About Market Risk. Any of our policies, strategies and activities may be modified or waived by our board of directors without stockholder consent. Developments in the market, which affect the policies and strategies mentioned herein or which change our assessment of the market, may cause our board of directors to revise our policies and financing strategies.

We have elected to qualify as a REIT for tax purposes. We have adopted certain compliance guidelines, which include restrictions on the acquisition, holding and sale of assets. Prior to the acquisition of any asset, we determine whether the asset meets REIT requirements. Substantially all of the assets that we have acquired and will acquire for investment are expected to qualify as REIT assets. This requirement limits our investment strategies.

The long-term investment operations primarily invest in Alt-A and multi-family mortgages and, to a lesser extent, B/C mortgages that are acquired from our mortgage operations. The long-term investment operation does not limit the proportion of its assets that may be invested in each type of mortgage.

We closely monitor our acquisition and investment in mortgage assets and the sources of our income, including income or expense from interest rate risk management strategies, to ensure at all times that we maintain our qualifications as a REIT. We have developed certain accounting systems and testing procedures to facilitate our ongoing compliance with the REIT provisions of the Internal Revenue Code. No changes in our investment policies and operating strategies, including credit criteria for mortgage asset investments, may be made without the approval of our board of directors.

We may at times and on terms that our board of directors deems appropriate:

- Issue senior securities - In December 1998, we issued $30.0 million of Series B 10.5% Convertible Preferred Stock. In February 2000, all shares of Series B Convertible Preferred Stock were exchanged for Series C 10.5% Cumulative Convertible Preferred Stock and the conversion rate was adjusted to $4.72 per share from $4.95 per share convertible into 5.29661 shares of common stock from 5.050505 shares of common stock. In August 2001, the shares of Series C Preferred Stock were converted to common stock;

Borrow money - We finance our operations in large part through the issuance of CMOs and short-term borrowings under reverse repurchase agreements. In addition, in March 1999, certain of our stockholders exchanged 1,359,507 shares of our common stock held by them, at an average price of $5.70 per share, for our 11% senior subordinated debentures due February 15, 2004. The debentures bore interest at 11% per annum and mature on February 15, 2004. In June 2001, we redeemed all of the debentures at a price equal to the face amount of the debentures plus accrued and unpaid interest;

Make loans to other persons - The warehouse lending operations provide reverse repurchase financing to affiliated companies and to approved non-affiliated clients, some of which are correspondents of the mortgage

operations, to finance mortgages during the time from the closing of the mortgages to their sale or other settlement with pre-approved investors;

Engage in the purchase and sale of investments - In connection with the issuance of mortgage-backed securities by our mortgage operations in the form of REMICs, our long-term investment operations may retain senior or subordinated securities on a short- or long-term basis;

Offer securities in exchange for property - In March 1999, certain of our stockholders exchanged 1,359,507 shares of their common stock at an average price of $5.70 per share for 11% senior subordinated debentures; and,

Repurchase or otherwise reacquire our shares or other securities in the future - During 2000, we adopted a repurchase plan to repurchase up to $3.0 million of our common stock in the open market. During 2001 and 2000, we repurchased 1,015,950 shares for $2.3 million. All repurchased shares were cancelled. During 2002 and 2003, we did not repurchase any shares of common stock. In February of 2004, the share repurchase program was cancelled by our board of directors.

We may also invest in securities of other issuers for the purpose of exercising control and underwrite the securities of other issuers, although we have not done so in the past and have no present intention to do so. Historically, we have and intend to continue to distribute annual reports to our stockholders, including financial statements audited by independent auditors, describing our current business and strategy.

Risk Factors

Some of the following risk factors relate to a discussion of our assets. For additional information on our asset categories refer to Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations, Note B Mortgages Held-for-Sale, Note C CMO Collateral, Note D Mortgages Held-for-Investment, and Note E Finance Receivables and in the accompanying notes to the consolidated financial statements.

Risks Related To Our Businesses

A prolonged economic downturn or recession would likely result in a reduction of our mortgage origination activity which would adversely affect our financial results.

The United States economy has undergone and may in the future, undergo, a period of slowdown, which some observers view as a recession. An economic downturn or a recession may have a significant adverse impact on our operations and our financial condition. For example, a reduction in new mortgages will adversely affect our ability to expand our long-term mortgage portfolio, our principal means of increasing our earnings. In addition, a decline in new mortgage activity will likely result in reduced activity for our warehouse lending operations and our long-term investment operations. In the case of our mortgage operations, a decline in mortgage activity may result in fewer loans that meet its criteria for purchase and securitization or sale, thus resulting in a reduction in interest income and fees and gain on sale of loans. We may also experience larger than previously reported losses on our long-term mortgage portfolio due to a higher level of defaults or foreclosures on our mortgages.

If we are unable to generate sufficient liquidity we will be unable to conduct our operations as planned.

If we cannot generate sufficient liquidity, we will be unable to continue to grow our operations, grow our asset base, maintain our current interest rate risk management policies and pay dividends. We have traditionally derived our liquidity from the following primary sources:

financing facilities provided to us by others to acquire or originate mortgage assets;

whole loan sales and securitizations of acquired or originated mortgages;

our issuance of equity and debt securities;

- excess cash flow from our long-term mortgage portfolio; and
- earnings from operations.

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. Our ability to meet our long-term liquidity requirements is subject to the renewal of our credit and repurchase facilities and/or obtaining other sources of financing, including additional debt or equity from time to time. Any decision by our lenders and/or investors to make additional funds available to us in the future will depend upon a number of factors, such as our compliance with the terms of our existing credit arrangements, our financial performance, industry and market trends in our various businesses, the lenders and/or investors own resources and policies concerning loans and investments, and the relative attractiveness of alternative investment or lending opportunities. If we cannot raise cash by selling debt or 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 growth of taxable income and also our ability to pay dividends.

Any significant margin calls under our financing facilities would adversely affect our liquidity and may adversely affect our financial results.

Prior to the fourth quarter of 1998, we generally had no difficulty in obtaining favorable financing facilities or in selling acquired mortgages. 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, too:

- the lack of financing to acquire these securitization interests;
- the widening of returns expected by institutional investors on securitization interests over the prevailing Treasury rate; and
- market uncertainty.

As a result, during this period many mortgage originators, including us, were unable to access the securitization market on favorable terms. This resulted in some companies declaring bankruptcy. Originators, like us, were required to sell loans on a whole loan basis and liquidate holdings of mortgage-backed securities to repay short-term borrowings. However, the large amount of mortgages available for sale on a whole loan basis affected the pricing offered for these mortgages, 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 were 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. Our current financing facilities continue to be short-term borrowings and we expect this to continue. 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.

We face risks related to our recent accounting restatements.

On July 22, 2004, we publicly announced that we had discovered accounting inaccuracies in previously reported financial statements. As a result, following consultation with our auditors, we decided to restate our financial statements for each of the years ended December 31, 2003, 2002 and 2001. The restatements relate to a correction to our revenue recognition policy with respect to the cash sales of mortgage servicing rights to unrelated third parties when the mortgage loans are retained, our accounting for derivatives and interest rate risk management activities, the accounting for loan purchase commitments as derivatives and selected elimination entries to consolidate IFC with that of IMH. The increase (decrease) in net earnings as a result of the net effect of the restatements for each of the years in the three-year period ended December 31, 2003 was $21.7 million, $(34.6) million and $(35.4) million, respectively.

The restatement of these financial statements may lead to litigation claims and/or regulatory proceedings against us. The defense of any such claims or proceedings may cause the diversion of management s attention and resources, and we may be required to pay damages if any such claims or proceedings are not resolved in our favor. Any litigation or regulatory proceeding, even if resolved in our favor, could cause us to incur significant legal and other expenses. We also may have difficulty raising equity capital or obtaining other financing, such as lines of credit or otherwise. We may not be able to effectuate our current operating strategy, including the ability to originate, acquire or securitize mortgages loans for retention or sale at projected levels. We may be subject to the resignation of our current external auditors which may, among other things, cause a delay in the preparation of our financial statements and increase expenditures related to the retention of new external auditors and the lead time required to become familiar with our operations. Moreover, we may be the subject of negative publicity focusing on the financial statement inaccuracies and resulting restatement and negative reactions from our stockholders, creditors or others with which we do business. The occurrence of any of the foregoing could harm our business and reputation and cause the price of our securities to decline.

If we fail to maintain an effective system of internal and disclosure controls, we may not be able to accurately report our financial results or prevent fraud. As a result, current and potential stockholders could lose confidence in our financial reporting which would harm our business and the trading price of our securities.

Effective internal and disclosure controls are necessary for us to provide reliable financial reports and effectively prevent fraud and to operate successfully as a public company. If we cannot provide reliable financial reports or prevent fraud, our reputation and operating results would be harmed. We have in the past discovered, and may in the future discover, areas of our disclosure and internal controls that need improvement. As a result after a review of our June 30, 2004 operating results, we identified certain deficiencies in some of our disclosure controls and procedures which we believe require remediation.

Furthermore, in planning and performing its audit of our restated consolidated financial statements, our external auditors also noted in a letter to management and the audit committee dated August 16, 2004 certain matters involving internal controls and operations that they consider to be a material weakness. According to the letter, we need to improve the evaluation and documentation of accounting policies and procedures for complex transactions, such as transfers of financial assets, derivatives and hedge accounting and allowance for credit losses, and we currently do not have a sufficient amount or type of staff in the financial reporting and accounting departments, including the lack of a Controller. Furthermore, our auditors noted significant deficiencies, as defined by the Public Company Accounting Oversight Board (PCAOB), for our consideration stating that our internal audit function does not provide an adequate or effective monitoring of our controls and we need to evaluate whether we have appropriate internal resources to manage and monitor work performed by our outsourced tax compliance function. We are currently taking steps to address these conditions, but we may be hampered in this regard by our current staffing.

We cannot be certain that our efforts to improve our internal and disclosure controls will be successful or that we will be able to maintain adequate controls over our financial processes and reporting in the future. Any failure to develop or maintain effective controls or difficulties encountered in their implementation or other effective improvement of our internal and disclosure controls could harm our operating results or cause us to fail to meet our reporting obligations. If we are unable to adequately establish or improve our internal controls over financial reporting, our external auditors may not be able to issue an unqualified opinion on the effectiveness of our internal controls. Ineffective internal and disclosure controls could also cause investors to lose confidence in our reported financial information, which would likely have a negative effect on the trading price of our securities.

We incurred losses for fiscal years 1997, 1998, 2000 and 2001 and may incur losses in the future.

During the years ended December 31, 2001 and 2000, we experienced a net loss of $2.2 million and $54.5 million. The 2001 loss was related to the mark-to-market loss on derivatives and the 2000 loss was the result of write-downs of non-performing investment securities secured by mortgages and additional increases in the provision for loan losses to provide for the deterioration of the performance of collateral supporting

specific investment securities for 2000. During the year ended December 31, 1998, we experienced a net loss of $5.9 million primarily as the mortgage industry experienced substantial turmoil as a result of a lack of liquidity in the secondary markets, which caused us to sell mortgages at losses to meet margin calls on our financing facilities. During the year ended December 31, 1997, we experienced a net loss of $16.0 million. The net loss incurred during 1997 included an accounting charge of $44.4 million that was the result of expenses related to the termination and buyout of our management agreement with

Imperial Credit Advisors, Inc. We cannot be certain that revenues will remain at current levels or improve or that we will be profitable or generate taxable income for distribution to our stockholders in the future, which could prevent us from effectuating our business strategy.

If we are unable to complete securitizations or if we experience delayed mortgage loan sales or securitization closings, we could face a liquidity shortage which would adversely affect our operating results.

We rely significantly upon securitizations to generate cash proceeds to repay borrowings and replenish our borrowing capacity. If there is a delay in a securitization closing or any reduction in our ability to complete securitizations we may be required to utilize other sources of financing, which, if available at all, may be on unfavorable terms. In addition, delays in closing mortgage sales or securitizations of our mortgages increase our risk by exposing us to credit and interest rate risks for this extended period of time. Furthermore, gains on sales from certain of our securitizations represent a significant portion of our taxable income. Several factors could affect our ability to complete securitizations of our mortgages, including:

- conditions in the securities and secondary markets;
- credit quality of the mortgages acquired or originated through our mortgage operations;
- volume of our mortgage loan acquisitions and originations;
- our ability to obtain credit enhancements; and
- lack of investors purchasing higher risk components of the securities.

If we are unable to sell a sufficient number of mortgages at a premium or profitably securitize a significant number of our mortgages in a particular financial reporting period, then we could experience lower income or a loss for that period, which could have a material adverse affect on our operations. We cannot assure you that we will be able to continue to profitably securitize or sell our loans on a whole loan basis, or at all.

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

Our borrowings and use of substantial leverage may cause losses.

Our use of CMOs may expose our operations to credit losses.

To grow our long-term mortgage portfolio, we borrow a substantial portion of the market value of substantially all of our investments in mortgages in the form of CMOs. There are no limitations on the amount of CMO financing we may incur, other than the aggregate value of the underlying mortgages. We currently use CMOs as financing vehicles to increase our leverage, since mortgages held for CMO collateral are retained for investment rather than sold in a secondary market transaction.

Retaining mortgages as collateral for CMOs exposes our operations to greater credit losses than does the use of other securitization techniques that are treated as sales because as the equity holder in the security, we are allocated losses from the liquidation of defaulted loans first prior to any other security holder. Although our liability under a collateralized mortgage obligation is limited to the collateral used to create the collateralized mortgage obligation, we generally are required to make a cash equity investment to fund collateral in excess of the amount of the securities issued in order to obtain the appropriate credit ratings for the securities being sold, and therefore obtain the lowest interest rate available, on the CMOs. If we experience greater credit losses than expected on the pool of loans subject to the CMO, the value of our equity investment will decrease and we may have to increase the allowance for loan losses on our financial statements.

Table of Contents

If we default under our financing facilities, we may be forced to liquidate collateral.

If we default under our financing facilities, our lenders could force us to liquidate the collateral. If the value of the collateral is less than the amount borrowed, we could be required to pay the difference in cash. Furthermore, if we default under one facility, it would generally cause a default under our other facilities. 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 or nothing at all.

If we are forced to liquidate, we may have few unpledged assets for distribution to unsecured creditors.

We have pledged a substantial portion of our assets to secure the repayment of CMOs issued in securitizations and our financing facilities. We will also pledge substantially all of our current and future mortgages to secure borrowings pending their securitization or sale. The cash flows we receive from our investments that have not yet been distributed or pledged or used to acquire mortgages or other investments may be the only unpledged assets available to our unsecured creditors if we were liquidated.

Interest rate fluctuations may adversely affect our operating results.

Our operations, as a mortgage loan acquirer and originator or a warehouse lender, may be adversely affected by rising and falling interest rates. Interest rates have been low over the past few years; however any increase in 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 or originated by our mortgage operations and decrease the demand for warehouse financing provided by our warehouse lending operations, which could adversely affect our operating results. 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 fixed and adjustable rate mortgages at lower long-term fixed interest rates. Increased loan prepayments could lead to a reduction in the number of loans in our long-term mortgage portfolio and reduce our net interest income. Rising interest rates may also increase delinquencies, foreclosures and losses on our adjustable rate mortgages.

We are subject to the risk of rising mortgage interest rates between the time we commit to purchase mortgages at a fixed price through the issuance of individual, bulk or other rate-locks 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 been sold or securitized or have not been properly hedged. As a result, we may record a smaller gain, or even a loss, upon the sale or securitization of those mortgages.

We may experience losses if our liabilities re-price at different rates than our assets.

Our principal source of revenue is net interest income or net interest spread from our long-term mortgage portfolio, 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 risk of loss.

Additionally, the rates paid on our borrowings and the rates received on our assets may be based upon different indices. If the index used to determine the rate on our borrowings, typically one-month LIBOR, increases faster than the indices used to determine the rates on our assets, such as six-month LIBOR or the prime rate, we will experience a declining net interest spread, which will have a negative effect on our profitability, and may result in losses.

An increase in our adjustable interest rate borrowings may decrease the net interest margin on our adjustable rate mortgages.

Our long-term mortgage portfolio includes mortgages that are six-month LIBOR hybrid ARMs. These are mortgages with fixed interest rates for an initial period of time, after which they begin bearing interest based upon

short-term interest rate indices and adjust periodically. We generally fund mortgages with adjustable interest rate borrowings having interest rates that are indexed to short-term interest rates and adjust periodically at various intervals. To the extent that there is an increase in the interest rate index used to determine our adjustable interest rate borrowings and that increase is not offset by a corresponding increase in the rates at which interest accrues on our assets or by various interest rate hedges that we have in place at any given time, our net interest margin will decrease or become negative. We may suffer a net interest loss on our ARMs that have interest rate caps if the interest rates on our related borrowings increase.

ARMs 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. As a result, 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 ARMs would be capped. If this occurs, our net interest spread could be significantly reduced or we could suffer a net interest loss.

Increased levels of early prepayments of mortgages may accelerate our expenses and decrease our net income.

Mortgage prepayments generally increase on our ARMs when fixed mortgage interest rates fall below the then-current interest rates on outstanding ARMs. Prepayments on mortgages are also affected by the terms and credit grades of the mortgages, conditions in the housing and financial markets and general economic conditions. If we acquire mortgages at a premium and they are subsequently repaid, we must expense the unamortized premium at the time of the prepayment. We could possibly lose the opportunity to earn interest at a higher rate over the expected life of the mortgage. Also, if prepayments on mortgages 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 generally 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 the mortgages that we acquire at a premium prepay faster than originally projected, generally accepted accounting principles, or GAAP, require us to write down the remaining capitalized premium amounts at a faster speed than was originally projected, which would decrease our current net interest income.

We may be subject to losses on mortgages for which we do not obtain credit enhancements.

We do not obtain credit enhancements such as mortgage pool or special hazard insurance for all of our mortgages and investments. Generally, we require mortgage insurance on any mortgage with an LTV ratio greater than 80%. During the time we hold mortgages for investment, we are subject to risks of borrower defaults and bankruptcies and special hazard losses that are not covered by standard hazard insurance. If a borrower defaults on a mortgage 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 and any insurance proceeds available to us through the mortgage insurer. In addition, since defaulted mortgages, which under our financing arrangements are mortgages that are generally 60 to 90 days delinquent in payments, may be considered negligible collateral under our borrowing arrangements, we could bear the risk of being required to own these loans without the use of borrowed funds until they are ultimately liquidated or possibly sold at a loss.

Our mortgage products expose us to greater credit risks.

We are an acquirer and originator of Alt-A mortgages, and to a lesser extent, multi-family and B/C mortgages. These are mortgages that generally may not qualify for purchase by government-sponsored agencies such as Fannie Mae and Freddie Mac. Our operations may be negatively affected due to our investments in these mortgages. Credit risks associated with these mortgages may be greater than those associated with conforming mortgages. The interest rates we charge on these mortgages are often higher than those charged for conforming loans in order to compensate for the higher risk and lower liquidity. Lower levels of liquidity may cause us to hold loans or other mortgage-related assets supported by these loans that we otherwise would not hold. By doing this, we assume the potential risk of increased delinquency rates and/or credit losses as well as interest rate risk. Additionally, 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.

Lending to our type of borrowers may expose us to a higher risk of delinquencies, foreclosures and losses.

Our market includes borrowers who may be unable to obtain mortgage financing from conventional mortgage sources. Mortgages made to such borrowers generally entail a higher risk of delinquency and higher losses than mortgages made to borrowers who utilize conventional mortgage sources. Delinquency, foreclosures and losses generally increase during economic slowdowns or recessions. The actual risk of delinquencies, foreclosures and losses on mortgages made to our borrowers could be higher under adverse economic conditions than those currently experienced in the mortgage lending industry in general.

Further, any material decline in real estate values increases the LTV ratios of mortgages previously made by us, thereby weakening collateral coverage and increasing the possibility of a loss in the event of a borrower default. Any sustained period of increased delinquencies, foreclosures or losses after the mortgages are sold could adversely affect the pricing of our future loan sales and our ability to sell or securitize our mortgages in the future. In the past, certain of these factors have caused revenues and net income of many participants in the mortgage industry, including us, to fluctuate from quarter to quarter.

Our multi-family mortgages expose us to increased lending risks.

Generally, we consider multi-family mortgages to involve a higher degree of risk compared to first mortgages on one- to four-family, owner occupied residential properties. These mortgages have higher risks than mortgages secured by residential real estate because repayment of the mortgages often depends on the successful operations and the income stream of the borrowers. Furthermore, multi-family mortgages typically involve larger mortgage balances to single borrowers or groups of related borrowers compared to one- to four-family residential mortgages.

Our use of second mortgages exposes us to greater credit risks.

Our security interest in the property securing second mortgages is subordinated to the interest of the first mortgage holder and the second mortgages have a higher combined LTV ratio than does the first mortgage. 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, our second mortgage loan will not be repaid.

The geographic concentration of our mortgages increases our exposure to risks in those areas.

We do not set limitations on the percentage of our long-term mortgage 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. Historically, a majority of our mortgage acquisitions and originations, long-term mortgage portfolio and finance receivables were secured by properties in California and, to a lesser extent, Florida. For instance, certain parts of California have experienced an economic downturn in past years and California and Florida have suffered the effects of certain natural hazards. Declines in those residential real estate markets may reduce the values of the properties collateralizing the mortgages, increase foreclosures and losses and have material adverse effect on our results of operations or financial condition.

Furthermore, if borrowers are not insured for natural disasters, which are typically not covered by standard hazard insurance policies, then they may not be able to repair the property or may stop paying their mortgages if the property is damaged. This would cause increased foreclosures and decrease our ability to recover losses on properties affected by such disasters. This would have a material adverse effect on our results of operations or financial condition.

Representations and warranties made by us in our loan sales and securitizations may subject us to liability.

In connection with our securitizations, we transfer mortgages acquired and originated by us into a trust in exchange for cash and, in the case of a CMO, residual certificates issued by the trust. The trustee will have recourse to us with respect to the breach of the standard representations and warranties made by us at the time such mortgages are transferred. While we generally have recourse to our customers for any such breaches, there can be no assurance of our customers abilities to honor their respective obligations. Also, we engage in bulk whole loan sales pursuant to agreements that generally provide for recourse by the purchaser against us in the event of a breach of one of our representations or warranties, any fraud or misrepresentation during the mortgage origination process, or upon early

default on such mortgage. We generally limit the potential remedies of such purchasers to the potential remedies we receive from the customers from whom we acquired or originated the mortgages. However, in some cases, the remedies available to a purchaser of mortgages from us may be broader than those available to us against the sellers of the mortgages and should a purchaser enforce its remedies against us, we may not always be able to enforce whatever remedies we have against our customers. Furthermore, if we discover, prior to the sale or transfer of a loan, that there is any fraud or misrepresentation with respect to the mortgage and the originator fails to repurchase the mortgage, then we may not be able to sell the mortgage or we may have to sell the mortgage at a discount.

In the ordinary course of our business, we are subject to claims made against us by borrowers and trustees in our securitizations arising from, among other things, losses that are claimed to have been incurred as a result of alleged breaches of fiduciary obligations, misrepresentations, errors and omissions of our employees, officers and agents (including our appraisers), incomplete documentation and our failure to comply with various laws and regulations applicable to our business. Any claims asserted against us may result in legal expenses or liabilities that could have a material adverse effect on our results of operations or financial condition.

A substantial interruption in our use of iDASLg2 may adversely affect our level of mortgage acquisitions and originations.

We utilize the Internet in our business principally for the implementation of our automated mortgage origination program, iDASLg2. iDASLg2 allows our customers to pre-qualify borrowers for various mortgage programs based on criteria requested from the borrower and renders an automated underwriting decision by issuing an approval of the mortgage loan or a referral for further review or additional information. Substantially, all of our correspondents submit mortgages through iDASLg2 and all wholesale mortgages delivered by mortgage bankers and brokers are directly underwritten through the use of iDASLg2. iDASLg2 may be interrupted if the Internet experiences periods of poor performance, if our computer systems or the systems of our third-party service providers contain defects, or if customers are reluctant to use or have inadequate connectivity to the Internet. Increased government regulation of the Internet could also adversely affect our use of the Internet in unanticipated ways and discourage our customers from using our services. If our ability to use the Internet in providing our services is impaired, our ability to originate or acquire mortgages on an automated basis could be delayed or reduced. Furthermore, we rely on a third party hosting company in connection with the use of iDASLg2. If the third party hosting company fails for any reason, and adequate back-up is not implemented in a timely manner, it may delay and reduce those mortgage acquisitions and originations done through iDASLg2. Any substantial delay and reduction in our mortgage acquisitions and originations will reduce our taxable income for the applicable period.

We are subject to risks of operational failure that are beyond our control.

Substantially all of our operations are located in Newport Beach, California and San Diego, California. Our systems and operations are vulnerable to damage and interruption from fire, flood, telecommunications failure, break-ins, earthquake and similar events. Our operations may also be interrupted by power disruptions, including rolling black-outs implemented in California due to power shortages. We do not maintain alternative power sources. Furthermore, our security mechanisms may be inadequate to prevent security breaches to our computer systems, including from computer viruses, electronic break-ins and similar disruptions. Such security breaches or operational failures could expose us to liability, impair our operations, result in losses, and harm our reputation.

Competition for mortgages is intense and may adversely affect our operations.

We compete in acquiring and originating Alt-A, B/C and multi-family mortgages 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 and brokers, insurance companies, other lenders, and other entities purchasing mortgage assets.

We also face intense competition from Internet-based lending companies where entry barriers are relatively low. Some of our competitors are much larger than we are, have better name recognition than we do, and have far greater financial and other resources. Government-sponsored entities, in particular Fannie Mae and Freddie Mac, are also expanding their participation in the Alt-A mortgage industry. These government-sponsored entities have a size and cost-of-funds advantage over us that allows them to price mortgages at lower rates than we are able to offer. This phenomenon may seriously destabilize the Alt-A mortgage industry. In addition, if as a result of what may be

less-conservative, risk-adjusted pricing, these government-sponsored entities experience significantly higher-than-expected losses, it would likely adversely affect overall investor perception of the Alt-A and B/C mortgage industry because the losses would be made public due to the reporting obligations of these entities.

The intense competition in the Alt-A, B/C and multi-family mortgage industry has also led to rapid technological developments, evolving industry standards and frequent releases of new products and enhancements. As mortgage products are offered more widely through alternative distribution channels, such as the Internet, we may be required to make significant changes to our current retail and wholesale structure and information systems to compete effectively. Our inability to continue enhancing our current Internet capabilities, or to adapt to other technological changes in the industry, could have a material adverse effect on our business, financial condition, liquidity and results of operations.

The need to maintain mortgage loan volume in this competitive environment creates a risk of price competition in the Alt-A, B/C and multi-family mortgage industry. Competition in the industry can take many forms, including interest rates and costs of a loan, less stringent underwriting standards, convenience in obtaining a loan, customer service, amount and term of a loan and marketing and distribution channels. Price competition would lower the interest rates that we are able to charge borrowers, which would lower our interest income. Price-cutting or discounting reduces profits and will depress earnings if sustained for any length of time. If our competition uses less stringent underwriting standards we will be pressured to do so as well, resulting in greater loan risk without being able to price for that greater risk. Our competitors may lower their underwriting standards to increase their market share. If we do not relax underwriting standards in the face of competition, we may lose market share. Increased competition may also reduce the volume of our loan originations and acquisitions. Any increase in these pricing and credit pressures could have a material adverse effect on our business, financial condition, liquidity and results of operations.

We are exposed to potential credit losses 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 bankers, including the risks of fraud, borrower default and bankruptcy, any of which could result in credit losses for us. Fraud risk may include the financing of nonexistent loans or fictitious mortgage loan transactions that could result in the loss of all sums we have advanced to the borrower. Also, our claims as a secured lender in a bankruptcy proceeding may be subject to adjustment and delay.

Our operating results will be affected by the results of our interest rate risk management activities.

To offset the risks associated with our mortgage operations, we enter into transactions designed to limit our exposure to interest rate risks. To offset the risks associated with adjustable rate borrowings, we attempt to match the interest rate sensitivities of our ARMs with the associated financing liabilities. Management determines the nature and quantity of derivative transactions based on various factors, including market conditions and the expected volume of mortgage acquisitions. While we believe that we properly manage our interest rate risk on an economic and tax basis, we are not able to apply hedge accounting, as established by the Financial Accounting Standards Board, or FASB, under the provisions of Statement of Financial Accounting Standards No. 133, or SFAS 133, for our interest rate risk management activities in our financial statements. The effect of not applying hedge accounting means that our interest rate risk management activities may result in significant volatility in our quarterly earnings as interest rates go up or down. It is possible that there will be periods during which we will incur losses on derivative transactions that may result in net losses, as was the case in 2001 after the restatement of our consolidated financial statements. In addition, if the counter parties to our derivative transactions are unable to perform according to the terms of the contracts, we may incur losses. While we believe we prudently manage interest rate risk, our derivative transactions may not offset the risk of adverse changes in net interest margins.

A reduction in the demand for our loan products may adversely affect our operations.

The availability of sufficient mortgages 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 residential mortgages, which is affected by:

- interest rates;
- national economic conditions;

residential property values; and

regulatory and tax developments.

If our mortgage acquisitions and originations decline, we may have:

decreased economies of scale;

higher origination costs per loan;

reduced fee income;

smaller gains on the sale of mortgages; and

an insufficient volume of mortgages to generate securitizations which thereby causes us to accumulate mortgages over a longer period.

Our delinquency ratios and our performance may be adversely affected by the performance of parties who service or sub-service our mortgages.

We sell or contract with third-parties for the servicing of all mortgages, including those in our securitizations. Our operations are subject to risks associated with inadequate or untimely servicing. Poor performance by a servicer may result in greater than expected delinquencies and losses on our mortgages. 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 mortgages subject to a securitization, greater delinquencies would adversely impact the value of our equity interest, if any, we hold in connection with that securitization.

In a securitization, relevant agreements permit us to be terminated as servicer or master servicer under specific conditions described in these agreements. If, as a result of a servicer or sub-servicer s failure to perform adequately, we were terminated as master servicer of a securitization, the value of any master servicing rights held by us would be adversely affected.

We are a defendant in purported class actions and may not prevail in these matters.

Class action lawsuits and regulatory actions alleging improper marketing practices, abusive loan terms and fees, disclosure violations, improper yield spread premiums and other matters are risks faced by all mortgage originators, particularly those in the Alt-A and B/C market. We are a defendant in purported class actions pending in different states. The class actions allege generally that the loan originator improperly charged fees in violation of various state lending or consumer protection laws in connection with mortgages that we acquired. Although the suits are not identical, they generally seek unspecified compensatory damages, punitive damages, pre- and post-judgment interest, costs and expenses and rescission of the mortgages, as well as a return of any improperly collected fees. The other purported class action claims damages for sending out unsolicited faxes and seeks statutory and treble damages. These actions are in the early stages of litigation and, accordingly, it is difficult to predict the outcome of these matters. We believe we have meritorious defenses to the actions and intend to defend against them vigorously; however, an adverse judgment in any of these matters could have a material adverse effect on us.

Regulatory Risks

We may be subject to fines or other penalties based upon the conduct of our independent brokers or correspondents.

The mortgage brokers and correspondents from which we obtain mortgages have parallel and separate legal obligations to which they are subject. While these laws may not explicitly hold the originating lenders responsible for the legal violations of mortgage bankers and brokers, increasingly federal and state agencies have sought to impose such liability. Previously, for example, the United States Federal Trade Commission, or FTC, entered into a settlement agreement with a mortgage lender where the FTC characterized a broker that had placed all of its loan production with a single lender as the agent of the lender; the FTC imposed a fine on the lender in part because, as principal, the

lender was legally responsible for the mortgage broker s unfair and deceptive acts and practices. The United States Justice Department in the past has sought to hold a sub-prime mortgage lender responsible for the pricing practices of its mortgage bankers and brokers, alleging that the mortgage lender was directly responsible for the total fees and charges paid by the borrower under the Fair Housing Act even if the lender neither dictated what the mortgage banker could charge nor kept the money for its own account. Accordingly, we may be subject to fines or other penalties based upon the conduct of our independent mortgage bankers and brokers or correspondents.

Violation of various federal, state and local laws may result in losses on our loans.

Applicable state and local laws generally regulate interest rates and other charges, require certain disclosure, and require licensing of the lender. In addition, other state and local laws, public policy and general principles of equity relating to the protection of consumers, unfair and deceptive practices and debt collection practices may apply to the origination, servicing and collection of our loans. Mortgage loans are also subject to federal laws, including:

- the Federal Truth-in-Lending Act and Regulation Z promulgated thereunder, which require certain disclosures to the borrowers regarding the terms of the loans;
- the Equal Credit Opportunity Act and Regulation B promulgated thereunder, which prohibit discrimination on the basis of age, race, color, sex, religion, marital status, national origin, receipt of public assistance or the exercise of any right under the Consumer Credit Protection Act, in the extension of credit;
- the Fair Credit Reporting Act, which regulates the use and reporting of information related to the borrower s credit experience;
- the Depository Institutions Deregulation and Monetary Control Act of 1980, which preempts certain state usury laws; and
- the Alternative Mortgage Transaction Parity Act of 1982, which preempts certain state lending laws which regulate alternative mortgage transactions.

Violations of certain provisions of these federal and state laws may limit our ability to collect all or part of the principal of or interest on the loans and in addition could subject us trust to damages and administrative enforcement and could result in the mortgagors rescinding the loans whether held by us or subsequent holders of the loans.

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 mortgages, 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 SEC 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 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.

New regulatory laws affecting the mortgage industry may increase our costs and decrease our mortgage origination and acquisition.

The regulatory environments in which we operate have an impact on the activities in which we may engage, how the activities may be carried out, and the profitability of those activities. Therefore, changes to laws, regulations or regulatory policies can affect whether and to what extent we are able to operate profitably. For example, recently

enacted and proposed local, state and federal legislation targeted at predatory lending could have the unintended consequence of raising the cost or otherwise reducing the availability of mortgage credit for those potential borrowers with less than prime-quality credit histories, thereby resulting in a reduction of otherwise legitimate Alt-A or B/C lending opportunities. Similarly, recently enacted and proposed local, state and federal privacy laws and laws prohibiting or limiting marketing by telephone, facsimile, email and the Internet may limit our ability to market and our ability to access potential loan applicants. For example, the recently enacted Can Spam Act of 2003 establishes the first national standards for the sending of commercial email allowing, among other things, unsolicited commercial email provided it contains certain information and an opt-out mechanism. We cannot provide any assurance that the proposed laws, rules and regulations, or other similar laws, rules or regulations, will not be adopted in the future. Adoption of these laws and regulations could have a material adverse impact on our business by substantially increasing the costs of compliance with a variety of inconsistent federal, state and local rules, or by restricting our ability to charge rates and fees adequate to compensate us for the risk associated with certain loans.

Some states and local governments have enacted, or may enact, laws or regulations that prohibit inclusion of some provisions in mortgage loans that have mortgage rates or origination costs in excess of prescribed levels, and require that borrowers be given certain disclosures prior to the consummation of such mortgage loans. Our failure to comply with these laws could subject us to monetary penalties and could result in the borrowers rescinding the mortgage loans, whether held by us or subsequent holders. Lawsuits have been brought in various states making claims against assignees of these loans for violations of state law.

Risks Related To Our Status As A REIT

We may not pay dividends to stockholders.

REIT provisions of the Internal Revenue Code generally require that we annually distribute to our stockholders at least 90% of all of our taxable income, exclusive of the application of any tax loss carry forwards that may be used to offset current period taxable income. These provisions restrict our ability to retain earnings and thereby generate capital from our operating activities. We may decide at a future date to terminate our REIT status, which would cause us to be taxed at the corporate levels and cease paying regular dividends. In addition, for any year that we do not generate taxable income, we are not required to declare and pay dividends to maintain our REIT status. For instance, due to losses incurred in 2000, we did not declare any dividends from September 2000 until September 2001.

To date, a portion of our taxable income and cash flow has been attributable to our receipt of dividend distributions from the mortgage operations. The mortgage operations is not a REIT and is not, therefore, subject to the above-described REIT distribution requirements. Because the mortgage operations is seeking to retain earnings to fund the future growth of our mortgage operations business, its board of directors may decide that the mortgage operations should cease making dividend distributions in the future. This would materially reduce the amount of our taxable income and in turn, would reduce the amount we would be required to distribute as dividends.

If we fail to maintain our REIT status, we may be subject to taxation as a regular corporation.

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.

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. 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 may 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 stockholders would be reduced substantially for each of the years involved. Failure to qualify as a REIT could adversely affect the value of our securities.

Table of Contents

Potential characterization of distributions or gain on sale as unrelated business taxable income to tax-exempt investors.

If (1) all or a portion of our assets are subject to the rules relating to taxable mortgage pools, (2) we are a pension-held REIT, (3) a tax-exempt stockholder has incurred debt to purchase or hold our common stock, or (4) the residual REMIC interests we buy generate excess inclusion income, then a portion of the distributions to and, in the case of a stockholder described in (3), 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 or certain of our stockholders to increased taxation.

If we have borrowings with two or more maturities and, (1) those borrowings are secured by mortgages 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 and the pool of mortgages or mortgage-backed securities to which such borrowings relate may be classified as a taxable mortgage pool under the Internal Revenue Code. If any part of our Company were to be treated as a taxable mortgage pool, then our REIT status would not be impaired, but a portion of the taxable income we recognize may, under regulations to be issued by the Treasury Department, be characterized as excess inclusion income and allocated among our stockholders to the extent of and generally in proportion to the distributions we make to each stockholder. 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).

Based on advice of our tax counsel, we take the position that our existing financing arrangements do not create a taxable mortgage pool.

We may be subject to possible adverse consequences as a result of limits on ownership of our shares.

Our charter limits ownership of our capital stock by any single stockholder to 9.5% of our outstanding shares unless waived by the board of directors. Our board of directors may increase the 9.5% ownership limit. In addition, to the extent consistent with the REIT provisions of the Internal Revenue Code, our board of directors may, pursuant to our articles of incorporation, waive the 9.5% ownership limit for a stockholder or purchaser of our stock. In order to waive the 9.5% ownership limit our board of directors must require the stockholder requesting the waiver to provide certain representations to the Company to ensure compliance with the REIT provisions of the Internal Revenue Code. 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 more than 50% (by value) 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;

26

may redeem the shares; and

will consider the shares held in trust for the benefit of a charitable beneficiary as designated by us.

Notwithstanding the above, we recently amended our charter so that nothing in the charter will preclude the settlement of transactions entered into through the facilities of the New York Stock Exchange (NYSE).

The trustee shall sell the shares held in trust and the owner of the excess shares will be entitled to the lesser of:

(a) the price paid by the owner;

(b) if the owner did not purchase the excess shares, the closing price for the shares on the national securities exchange on which IMH is listed on the day of the event causing the shares to be held in trust; or

(c) the price received by the trustee from the sale of the shares.

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.

Risks Related To Ownership of Our Securities

Our share prices have been and may continue to be volatile.

Historically, the market price of our securities has been volatile. The market price of our securities is likely to continue to be highly volatile and could be significantly affected by factors including:

the amount of dividends paid;

availability of liquidity in the securitization market;

loan sale pricing;

termination of financing agreements;

margin calls by warehouse lenders or changes in warehouse lending rates;

unanticipated fluctuations in our operating results;

prepayments on mortgages;

valuations of securitization related assets;

the effect of the restatement of our financial condition and results of operations;

mark to market adjustments related to the fair value of derivatives;

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 securities of mortgage REIT 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 securities could also be materially adversely affected and we may experience difficulty in raising capital.

Table of Contents

Sales of additional common stock may adversely affect its market price.

To sustain our growth strategy we intend to raise capital through the sale of equity. 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. We do not know the actual or perceived effect of these offerings, the timing of these offerings, the potential 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. In December 2003, we filed a shelf registration statement for a total of $500.0 million, which may be used in connection with offerings of debt securities, common stock, preferred stock, warrants, and/or units for general corporate purposes. As of September 30, 2004, we may sell additional securities worth approximately $177.1 million (gross proceeds) from this shelf registration statement in the future. We also have shares reserved for future issuance under our stock plans. The sale of a large amount of shares or the perception that such sales may occur, could adversely affect the market price for our common stock or other outstanding securities.

ITEM 2. PROPERTIES

Our primary executive and administrative offices are located at 1401 Dove Street, Newport Beach, California where we have a premises lease expiring in May of 2008 to use approximately 74,000 square feet of office space. During October of 2003, we executed a premises lease located at 1500 Quail Street, Newport Beach, California expiring in November of 2006 to use approximately 15,000 square feet of office space to accommodate expansion. The mortgage operations has six mortgage production offices located in various states with premises lease terms ranging from month to month or one to two years. Novelle has offices located in San Diego, California with lease terms expiring in March 2005 for approximately 21,000 square feet of office space. We believe that these facilities will adequately provide for the near-term growth needs of our core operating businesses.

ITEM 3. LEGAL PROCEEDINGS

On September 1, 2000, a complaint captioned Michael P. and Shellie Gilmor v. Preferred Credit Corporation and Impac Funding Corporation, et al. was filed in the Circuit Court for Clay County, Missouri, Case No. CV100-4263-CC, as a purported class action lawsuit alleging that the defendants violated Missouri s Second Loans Act and Merchandising Practices Act. In July 2001, the Missouri complaint was amended to include IMH and other Impac-related entities. A plaintiffs class was certified on January 2, 2003.

On October 2, 2001, a complaint captioned Deborah Searcy, Shirley Walker, et al. v. Impac Funding Corporation, Impac Mortgage Holdings, Inc. et. al. was filed in the Wayne County Circuit Court, State of Michigan, as a purported class action lawsuit alleging that the defendants violated Michigan s Secondary Mortgage Loan Act, Credit Reform Act and Consumer Protection Act. A motion to dismiss the complaint has been filed.

On October 10, 2001, a complaint captioned Hayes v. Impac Funding Corporation, et al. was filed in the Circuit Court of Vanderburgh County, Indiana as Case No. 82C01-0110-CP580. This was stated as a purported class action lawsuit alleging a violation of the Indiana Uniform Consumer Credit Code when the loans were originated. This matter was dismissed as to the Impac defendants and the dismissal was affirmed by the Court of Appeals.

On November 30, 2001, a complaint captioned Garry Lee Skinner and Judy Cooper Skinner, et al. v. Preferred Credit, et al. was filed in the Superior Court of Durham County, North Carolina as Case No. 1CV-05596. This is stated as a purported class action alleging a violation of the North Carolina Interest Statutes and Unfair and Deceptive Trade Practices Act when the secondary mortgage loans were originated by the

defendants. A motion to dismiss the complaint has been filed. This motion remains pending.

On July 31, 2003, a purported class action complaint captioned Frazier, et al v. Impac Funding Corp., et al, Case No. 03-2565 was filed in federal court in Tennessee. The causes of action in the action allege violations of Tennessee s usury statute and Consumer Protection Act. A motion to dismiss the complaint has been filed.

On November 25, 2003, a complaint captioned Michael and Amber Stallings v. Empire Funding Home Loan Owner Trust 1997-3; U.S. Bank, National Association; and Wilmington Trust Company was filed in the United States District Court for the Western District of Tennessee, Case No. 03-2548, as a purported class action lawsuit alleging that the defendants violated Tennessee predatory lending laws governing second mortgage loans. The complaint further

alleges that certain assignees of mortgage loans, including two Impac-related trusts, should be included as defendants in the lawsuit.

On February 3, 2004, a complaint captioned James and Jill Baker v. Century Financial Group, Inc, et al was filed in the Circuit Court of Clay County, Missouri, Case No. CV100-4294-CC as a purported class action lawsuit alleging that the defendants violated Missouri s Second Loan Act and Merchandising Practices Act.

All of the above purported class action lawsuits are similar in nature in that they allege that the mortgage loan originators violated the respective state s statutes by charging excessive fees and costs when making second mortgage loans on residential real estate. The complaints allege that IFC was a purchaser, and is a holder, along with other affiliated entities, of second mortgage loans originated by other lenders. The plaintiffs in the lawsuits are seeking damages that include disgorgement, restitution, rescission, actual damages, statutory damages, exemplary damages, pre-judgement interest and punitive damages. No material dollar amount of damages are specified in the complaints.

On October 14, 2003, an action was filed in the Circuit Court of Cook County, Illinois as Case No. 03 CH17085 entitled Fast Forward Solutions, LLC v. Novelle Financial Services, Inc. The complaint contains allegation of a class action and alleges that the defendant sent out unsolicited faxes in violation of the Telephone Consumer Protection Act, the Illinois Consumer Fraud Act, and Illinois common law. The plaintiff is seeking statutory and treble damages.

We believe that we have meritorious defenses to the above claims and intend to defend these claims vigorously. Nevertheless, litigation is uncertain and we may not prevail in the lawsuits and can express no opinion as to its ultimate outcome. We are a party to other litigation and claims which are normal in the course of our operations. While the results of such other litigation and claims cannot be predicted with certainty, we believe the final outcome of such other matters will not have a material adverse effect on our financial condition or results of operations.

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 2003.

Table of Contents

PART II

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

On June 11, 2003, our common stock was listed and began trading on the New York Stock Exchange, or NYSE, under the symbol IMH. Prior to June 11, 2003, our common stock was listed on the American Stock Exchange under the same symbol. The following table summarizes the high, low and closing sales prices for our common stock for the periods indicated:

	2003			2002		
	High	**Low**	**Close**	**High**	**Low**	**Close**
First Quarter	$ 13.23	$ 11.05	$ 12.99	$ 9.55	$ 7.80	$ 9.42
Second Quarter	16.97	12.46	16.69	13.48	8.85	13.48
Third Quarter	16.55	12.50	16.19	13.10	8.16	11.15
Fourth Quarter	19.21	14.80	18.21	12.28	9.08	11.50

On March 10, 2004, the last reported sale price of our common stock on the NYSE was $22.62 per share. As of March 10, 2004, there were 566 holders of record, including holders who are nominees for an undetermined number of beneficial owners, of our common stock.

Securities Authorized for Issuance under Equity Compensation Plans. Refer to Item 12. Security Ownership of Certain Beneficial Owners and Management.

Dividend Distributions. To maintain our qualification as a REIT, we intend to make annual distributions to stockholders at an amount that maintains our REIT status in accordance with the Internal Revenue Code, which may not necessarily equal net earnings as calculated in accordance with GAAP. Our dividend policy is subject to revision at the discretion of the board of directors. All distributions in excess of those required to maintain our REIT status will be made at the discretion of the board of directors and will depend on our taxable income, financial condition and 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 or qualified income, although a portion of such distributions may be designated by us as capital gain or may constitute a tax-free return of capital. We annually furnish to each of our stockholders a statement setting forth distributions paid during the preceding year and their characterization as ordinary income, qualified income, capital gain or return of capital.

The following table presents our dividends paid or declared for the periods indicated:

Period Covered	**Stockholder Record Date**	**Per Share Dividend Amount**

Quarter ended March 31, 2002	April 3, 2002	$	0.40
Quarter ended June 30, 2002	July 3, 2002	$	0.43
Quarter ended September 30, 2002	October 2, 2002	$	0.45
Quarter ended December 31, 2002	January 2, 2003	$	0.48
Quarter ended March 31, 2003	April 4, 2003	$	0.50
Quarter ended June 30, 2003	July 3, 2003	$	0.50
Quarter ended September 30, 2003	October 3, 2003	$	0.50
Quarter ended December 31, 2003	December 15, 2003	$	0.55

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, 2003 and the consolidated balance sheet data for the five-year period ended December 31, 2003 were derived from the consolidated financial statements, as restated. 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.

Table of Contents

IMPAC MORTGAGE HOLDINGS, INC.

(dollar amounts in thousands, except per share data and operating data)

	For the year ended December 31,				
	2003 (1)	2002	2001	2000	1999
	(as restated, all periods)				
Statement of Operations Data:					
Net interest income:					
Interest income	$ 386,741	$ 230,267	$ 141,563	$ 119,277	$ 106,884
Interest expense	209,009	127,801	108,183	124,071	89,396
Net interest income (expense)	177,732	102,466	33,380	(4,794)	17,488
Provision for loan losses	24,853	19,848	16,813	18,839	5,547
Net interest income (expense) after loan loss provision	152,879	82,618	16,567	(23,633)	11,941
Non-interest income:					
Gain on sale of loans	39,022				
Equity in net earnings of IFC	11,537	11,299	19,499	24,461	15,727
Mark-to-market gain (loss) derivative instruments	(16,021)	(50,502)	(33,391)	238	
Other income	9,995	2,864	5,295	3,857	2,149
Total non-interest income (expense)	44,533	(36,339)	(8,597)	28,556	17,876
Non-interest expense:					
Personnel expense	25,250	1,856	1,192	652	473
General and administrative and other expenses	21,256	2,883	3,355	3,339	2,750
Write-down on securities available-for-sale	298	1,039	2,217	53,576	2,118
(Gain) loss on disposition of real estate owned	(2,632)	154	(1,931)	1,814	2,159
Total non-interest expense	44,172	5,932	4,833	59,381	7,500
Earnings (loss) before extraordinary item and cumulative effect of change in accounting principle	153,240	40,347	3,137	(54,458)	22,317
Extraordinary item			(1,006)		
Income taxes	4,261				
Cumulative effect of change in accounting Principle			(4,313)		
Net earnings (loss)	$ 148,979	$ 40,347	$ (2,182)	$ (54,458)	$ 22,317
Net earnings (loss) per share before extraordinary item and cumulative effect of change in accounting principle:					
Basic	$ 2.94	$ 1.01	$ 0.07	$ (2.71)	$ 0.83
Diluted	$ 2.88	$ 0.99	$ 0.11	$ (2.71)	$ 0.76
Net earnings (loss) per share:					
Basic	$ 2.94	$ 1.01	$ (0.16)	$ (2.71)	$ 0.83

Diluted	$	2.88	$	0.99	$	(0.16)	$	(2.71)	$	0.76
Dividends declared per share	$	2.05	$	1.76	$	0.69	$	0.36	$	0.48

Table of Contents

	As of December 31,				
	2003	2002	2001	2000	1999
	(as restated, all periods)				
Balance Sheet Data:					
Mortgages held-for-investment and CMO collateral	$ 9,291,828	$ 5,177,444	$ 2,224,413	$ 1,367,573	$ 1,293,580
Finance receivables	630,030	664,021	300,571	138,406	129,752
Mortgages held-for-sale	397,618				
Investment in and advances to IFC (1)		531,032	210,134	304,578	107,639
Total assets	10,577,957	6,540,339	2,842,677	1,884,489	1,663,536
CMO borrowings	8,489,853	5,019,934	2,139,818	1,277,161	838,924
Reverse repurchase agreements	1,568,807	1,168,029	469,491	398,653	539,687
Total liabilities	10,105,170	6,256,814	2,646,847	1,706,274	1,424,692
Total stockholders equity	472,787	283,525	195,830	178,214	238,844

(1) On July 1, 2003, IMH purchased 100% of the outstanding shares of common stock of IFC. The purchase of IFC s common stock combined with IMH s ownership of 100% of IFC s preferred stock resulted in the consolidation of IFC from July 1, 2003 through December 31, 2003. Prior to July 1, 2003, IFC was a non-consolidated subsidiary of IMH and 99% of the net earnings of IFC were reflected in IMH s financial statements as Equity in net earnings (loss) of IFC.

	As of and for the year December 31,				
	2003	2002	2001	2000	1999
Operating Data (in millions):					
Mortgage acquisitions and originations for the year	$ 9,525	$ 5,945	$ 3,204	$ 2,113	$ 1,672
Master servicing portfolio at period-end	13,919	8,694	5,569	4,043	2,879
Servicing portfolio at period-end	1,402	2,653	1,754	2,429	2,393

Table of Contents

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

Management s discussion and analysis of financial condition and results of operations contain certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Refer to Item 1. Business Forward-Looking Statements for a complete description of forward-looking statements. All of our businesses actively work together to deliver comprehensive mortgage and lending services to our correspondents, mortgage bankers and brokers, retail customers and capital market investors through a wide array of mortgage loan programs using web-based technology and centralized operations so that we can strive to provide high levels of customer service at low costs per loan. We elect to be taxed as a REIT for federal income tax purposes, which generally allows us to pass through income to stockholders without payment of federal income tax at the corporate level. Our goal is to generate consistent reliable income for distribution to our stockholders primarily from the earnings of our core operating businesses, which include the long-term investment operations, mortgage operations and warehouse lending operations. Refer to Item 1. Business for additional information on our businesses and operating segments.

Restatement of Consolidated Financial Statements

The consolidated balance sheets as of December 31, 2003 and 2002 and consolidated statements of operations and comprehensive earnings, consolidated statements of changes in stockholders equity and consolidated statements of cash flows for each of the years in the three-year period ended December 31, 2003 have been restated. The effect of this restatement on net earnings (loss) for each of the years in the three-year period ended December 31, 2003 was an increase (decrease) of $21.7 million, $(34.6) million and $(35.4) million, respectively.

For a further discussion of the corrections and restatements, see Explanatory Note at the beginning of this Form 10-K/A and Note A.2. Restatement of Consolidated Financial Statements in the accompanying notes to consolidated financial statements. The effect of the restatement of the consolidated financial statements is reflected in Management s Discussion and Analysis of Financial Condition and Results of Operations below.

Consolidation of IFC

On July 1, 2003, IMH entered into a stock purchase agreement with Joseph R. Tomkinson, our Chairman, Chief Executive Officer and a director, William S. Ashmore, our Chief Operating Officer, President and a director, and the Johnson Revocable Living Trust, of which Richard J. Johnson, our Executive Vice President and Chief Financial Officer is trustee, whereby we purchased all of the outstanding shares of voting common stock of IFC for aggregate consideration of $750,000. Each of Messer s. Tomkinson and Ashmore and the Johnson Revocable Living Trust owned one-third of the outstanding common stock of IFC. The fairness opinion related to the purchase price of IFC, as rendered by an independent financial advisor, and the subsequent transaction was approved by our board of directors. Prior to the July 1, 2003 acquisition, the common stock of IFC represents 1% of the economic interest in IFC and the outstanding non-voting preferred stock of IFC represents 99% of the economic interest in IFC. As a result of acquiring 100% of IFC s common stock on July 1, 2003, IMH owns all of the common stock and preferred stock of IFC and began to consolidate IFC as of that date. Due to the consolidation of IFC on July 1, 2003, the consolidated financial statements include the results of operations of the mortgage operations for the period from January 1, 2003 to June 30, 2003, or non-consolidation period, as equity in net earnings of IFC and for the period from July 1, 2003 to December 31, 2003, or consolidation period, on a consolidated basis. IMH has not consolidated the financial statements of IFC for the periods prior to July 1, 2003 to conform to the current presentation. Therefore, when comparing the consolidated financial statements for 2003 to 2002, it may appear that there are significant variances. This is partially due to the presentation of the financial information. In order to make comparative information meaningful, comparisons may require the presentation of certain financial information for IMH and IFC as stand-alone, when indicated.

Critical Accounting Policies

We define critical accounting policies as those that are important to the portrayal of our financial condition and results of operations and require estimates and assumptions based on our judgment of changing market conditions and the performance of our assets and liabilities at any given time. In determining which accounting policies meet this definition, we considered our policies with respect to the valuation of our assets and liabilities and estimates and assumptions used in determining those valuations. We believe the most critical accounting issues that require the most complex and difficult judgments and that are particularly susceptible to significant change to our financial condition and results of operations include the following:

- allowance for loan losses;

Table of Contents

derivative financial instruments; and

securitization of financial assets as financing versus sale.

Allowance for loan losses. We provide an allowance for loan losses for mortgages held as CMO collateral, finance receivables and mortgages held-for-investment, or loans provided for. In evaluating the adequacy of the allowance for loan losses, management takes several items into consideration. For instance, a detailed analysis of historical loan performance data is accumulated and reviewed. This data is analyzed for loss performance and prepayment performance by product type, origination year and securitization issuance. The results of that analysis are then applied to the current mortgage portfolio and an estimate is created. We believe that pooling of mortgages with similar characteristics is an appropriate methodology in which to evaluate the allowance for loan losses. In addition, management provides an allowance for loan losses for Alt-A mortgages that are retained for long-term investment and which are not underwritten to our specific underwriting guidelines. These mortgages are acquired on a bulk basis by the mortgage operations from other mortgage originators that underwrite mortgages substantially similar, but not specific, to our mortgage underwriting guidelines, or non-Impac mortgages. Management also recognizes that there are qualitative factors that must be taken into consideration when evaluating and measuring inherent loss in our loan portfolios. These items include, but are not limited to, economic indicators that may affect the borrower s ability to pay, changes in value of collateral, political factors and industry statistics. Specific valuation allowances may be established for loans that are deemed impaired, if default by the borrower is deemed probable, and if the fair value of the loan or the collateral is estimated to be less than the gross carrying value of the loan. Actual losses on loans are recorded as a reduction to the allowance through charge-offs. Subsequent recoveries of amounts previously charged off are credited to the allowance. For additional information regarding allowance for loan losses refer to Results of Operations and Financial Condition.

Derivative financial instruments. The mortgage operations acquire derivatives to mitigate changes in the value of its mortgage pipeline. The mortgage pipeline consists of mortgages that have not yet been acquired, however, the mortgage operations has committed to acquire the mortgages in the future at pre-determined interest rates through rate-lock commitments. On March 9, 2004, the SEC issued Staff Accounting Bulletin 105, Application of Accounting Principles to Loan Commitments, or SAB 105, which clarifies the SEC s position on the accounting and valuation for commitments to originate mortgage loans held-for-sale. Consistent with SFAS No. 149, Amendment of Statement 133 on Derivative Instruments and Hedging Activities, or SFAS 149, SAB 105 states that loan commitments are treated as derivatives. Prior to the issuance of SAB 105, the mortgage operations recorded the fair value of its mortgage pipeline, inclusive of changes in benchmark interest rates and acquisition premiums, as it qualifies as a derivative under the provisions of Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities, or SFAS 133, however, it does not qualify for hedging treatment. Therefore, the mortgage pipeline and the fair value of derivatives were marked to market each reporting period. SAB 105 requires that in valuing these loan commitments entities not include cash flows associated with servicing as to do so would result in the recognition of servicing assets prior to the sale or securitization of funded loans. This valuation methodology limits a company s ability to record an asset for its mortgage pipeline as of the applicable reporting date. Subsequent to SAB 105, as of April 1, 2004 we record the fair value change of the mortgage pipeline based solely on interest rate fluctuations from the date of rate-lock to the applicable reporting date. Other derivatives, as accounted for under SFAS 133 and which principally reduce exposure to interest rate risk associated with specific liabilities, are also carried at fair value with changes in fair value reflected in earnings.

Securitization of financial assets as financing versus sale. The mortgage operations recognize gains or losses on the sale of mortgages when the sales transaction settles or upon the securitization of the mortgages 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 related premiums received and costs associated with the acquisition or origination of mortgages. 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. The long-term investment operations structure CMO securitizations as financing arrangements and recognize no gain or loss on the transfer of mortgage assets. The CMO securitization trusts do not meet criteria within SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities (SFAS 140), to be qualifying special purpose entities, and further, are considered variable interest entities under FASB Interpretation No. 46R and, therefore, are consolidated by the long-term investment operations as the entities primary beneficiary. The mortgage operations structure REMIC securitizations as sales, and gains and losses are recognized. Liabilities and derivatives incurred or obtained at 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 and retained interest, management estimates future rates of prepayments,

prepayment penalties to be received, delinquencies, defaults and default loss severity and their impact on estimated cash flows.

Financial Highlights for 2003

- Estimated taxable income per share increased 19% to $2.46 compared to actual taxable income per share of $2.07 for 2002;
- Cash dividends declared in 2003 increased 16% to $2.05 per share compared to $1.76 per share for 2002;
- Total assets increased 63% to $10.6 billion at year-end from $6.5 billion as of prior year-end;
- Book value per share increased 34% to $8.39 at year-end compared to $6.26 as of prior year-end;
- Total market capitalization was approximately $1.0 billion at year-end compared to $521.2 million at prior year-end;
- Dividend yield as of December 31, 2003 was 12.08%, based on an annualized fourth quarter dividend of $0.55 per share and a closing stock price of $18.21;
- Total return to stockholders was 76% based on common stock price appreciation of $6.71 per share and common stock dividends declared of $2.05 per share;
- The mortgage operations acquired and originated $9.5 billion of primarily Alt-A mortgages, a 61% increase over $5.9 billion for 2002;
- The long-term investment operations retained $5.8 billion of Alt-A mortgages and originated $290.5 million of multi-family mortgages as compared to $3.9 billion and $25.8 million, respectively, for 2002; and
- Average finance receivables to non-affiliated clients increased 77% to $604.1 million compared to $341.5 million for 2002.

Taxable Income

After adjusting for our estimates of the differences between net earnings and taxable income, estimated taxable income was $127.5 million, or $2.46 per diluted share, for 2003 as compared to $84.4 million, or $2.07 per diluted share, for 2002 and $38.3 million, or $1.37 per diluted share, for 2001. When we file our annual tax returns there are certain adjustments that we make to net earnings and taxable income due to differences in the nature and extent that revenues and expenses are recognized under the two methods. As an example, to calculate taxable income we deduct actual loan losses as compared to the determination of net earnings that require a deduction of loan loss provisions which are determined based on estimated losses inherent in our mortgage portfolios. To maintain our REIT status, we are required to distribute a minimum of 90% of our annual taxable income to our stockholders. Because we pay dividends based on taxable income, dividends may be more or less than net earnings. As such, we believe that the disclosure of estimated taxable income, which is a non-generally accepted accounting principle, or GAAP, financial measurement, is useful information for our investors.

We paid total regular cash dividends of $2.53 per share in 2003, $1.76 per share in 2002 and $0.69 per share in 2001, which when combined with available tax loss carry forwards at the time met taxable income distribution requirements for each year. Upon the filing of our 2002 tax return, we had federal and state net operating tax loss carry-forwards of $18.7 million that may or may not be used to offset taxable income in 2003 or in subsequent years, which expire in the year 2020 and 2010, respectively.

Table of Contents

The following table presents a reconciliation of net earnings to estimated and actual taxable income for the periods indicated (in thousands, except per share amounts):

	For the year ended December 31,		
	2003 (1)	2002 (1)	2001 (1)
Net earnings	$ 148,979	$ 40,347	$ (2,182)
Adjustments to GAAP earnings:			
Loan loss provision	24,853	19,848	16,813
Dividends from IFC	31,385	12,870	8,894
Fair value of free-standing derivatives (2)	(38,762)	22,141	28,176
Tax deduction for actual loan losses	(12,859)	(4,938)	(10,211)
Net earnings of IFC (3)	(16,191)	(4,644)	(3,603)
Cash received from previously charged-off assets	(5,533)		
Tax loss on sale of investment securities	(4,725)		
Alternative minimum tax			550
Other miscellaneous adjustments	319	(1,267)	(112)
Estimated taxable income (4)	$ 127,466	$ 84,357	$ 38,325
Estimated taxable income per diluted share (4)	$ 2.46	$ 2.07	$ 1.37
Diluted weighted average shares outstanding	51,779	40,773	27,952

(1) 2003 is an estimate of taxable income. 2002 and 2001 are actual taxable income calculations per the filing of our corporate tax returns.

(2) The mark-to-market change for the valuation of free-standing derivatives is income or expense for GAAP financial reporting but is not included as an addition or deduction for taxable income calculations.

(3) Represents GAAP net earnings which may not necessarily equal taxable income. Therefore, dividend distributions from IFC to IMH may exceed GAAP net earnings.

(4) Excludes the deduction for dividends paid and the availability of a deduction attributable to net operating loss carryforwards. Additionally, 2002 and 2001 exclude annual tax deductions of approximately $11.0 million for amortization of the termination of our management agreement.

Results of Operations and Financial Condition

Review of 2003. Our expectation for 2003 was that the United States economy would gradually recover and expand over the year which would lead to higher interest rates. We believed that higher mortgage rates would, in turn, lead to a contraction of industry-wide mortgage activity, specifically, mortgage refinance activity, from mortgage origination levels experienced during 2002. To counter the expectation of a contracting mortgage origination market, we implemented strategies in early 2003 which we believed would result in relatively stable loan production levels during 2003 as compared to 2002. Our primary strategy was to increase our acquisition of non-Impac Alt-A mortgages. Borrowers of non-Impac Alt-A mortgages historically have higher credit scores than Impac Alt-A mortgages. We believe that by improving the overall credit quality of

our long-term mortgage portfolio we can more consistently generate a reliable stream of future cash flow and taxable income that can be distributed to our stockholders.

During 2003, the United States economy did not expand as we and the market expected. In response, the Federal Reserve Bank lowered short-term interest rates to spur economic growth, which led to a further decline in mortgage rates and created a second mortgage refinancing wave which exceeded that of 2002. The refinancing wave coupled with a strong residential construction and home purchase market and our acquisition of non-Impac mortgages resulted in record acquisitions and originations during 2003. Total loan production increased 61% to $9.5 billion during 2003 as compared to $5.9 billion during 2002. The mortgage operations acquired $2.2 billion of non-Impac Alt-A mortgages, or 23% of total mortgage production, during 2003 as compared to $164.6 million, or 3%, of total mortgage production, during 2002. Non-Impac Alt-A mortgages acquired during 2003 had an original weighted average credit score of 710 with an original weighted average LTV of 73% and an average loan size of $274,000. Impac mortgages acquired or originated during 2003 had an original weighted average credit score of 698 with an original weighted average LTV of 75% and an average loan size of $221,000.

2003 did present some challenges the most significant of which was mortgage prepayments as interest rates declined to historic lows during the first half of 2003, which was followed by a rapid rise in the 10-year Treasury yield during June and July of 2003. As a result of the increase in the 10-year Treasury yield, ARMs became more attractive to borrowers than traditional FRMs, which were refinanced at a record pace. However, due to our mortgage origination capabilities and our efficiency as an acquirer and originator of ARMs, we were able to replace the prepayment of seasoned mortgages with primarily new ARMs. Although ARMs declined to 58% of total mortgage production during 2003 as compared to 62% during 2002, ARMs accounted for 75% of total mortgage production during the fourth quarter of 2003 as compared to 53% during the third quarter of 2003 as the yield curve steepened.

The retention of mortgages for long-term investment during 2003 resulted in a 63% increase in total assets to $10.6 billion at year-end 2003. As of December 31, 2003, 81% of our long-term mortgage portfolio consisted of mortgages with active prepayment penalties and 86% were ARMs that had an original weighted average credit score of 694 and an original weighted average LTV of 79%. Mortgages retained for long-term investment were primarily financed through the issuance of CMOs and the sale of common stock. In November and December of 2003, we completed CMOs of approximately $1.0 billion each month, which provided long-term financing for mortgages primarily acquired and originated during the fourth quarter of 2003. Altogether, we completed $6.0 billion in CMOs during 2003 to finance the retention and origination of $6.1 billion of primarily Alt-A mortgages and multi-family mortgages. The use of CMO borrowings allows more efficient and effective utilization of available capital and investment in our operating businesses at favorable returns while having to raise less capital than may be required with other financing sources, such as reverse repurchase borrowings. In addition, we raised net cash proceeds of $150.4 million through the sale of common stock during 2003. The issuance of new shares of common stock was accretive to book value, which increased 34% to $8.39 per share at year-end 2003 as compared to $6.26 as of prior year-end.

Other accomplishments during 2003 include a 51% increase in estimated taxable income, 76% total annual return to stockholders, market capitalization over $1.0 billion and we began trading on the NYSE. Our success in ever-changing interest rate environments and mortgage origination cycles is a testament to our flexibility and efficiency as an originator, acquirer, seller and investor in both fixed rate and adjustable rate mortgages and the operating synergies of our various business units within our organizational structure.

Outlook for 2004. Our interest rate bias for 2004 is much the same as 2003. We expect gradually increasing short-term interest rates as economic activity improves. We have seen a significant shift from FRMs to ARMs during the third and fourth quarters of 2003, as well as in our mortgage pipeline, as long-term interest rates trended higher during the last half of 2003. As a result of this trend, we expect to acquire and originate a higher percentage of our overall mortgage production in ARMs throughout 2004. In order to maintain our strategy of retaining all ARMs and continue growing our balance sheet in 2004, we anticipate that we will need to raise additional cash through the issuance of new shares of common stock. As a result of planned growth, we filed a universal shelf registration statement with the SEC to issue up to $500.0 million of new securities, which became effective in January of 2004. In February 2004, we issued 5,750,000 new shares from the universal shelf and raised net cash proceeds of $106.5 million.

Although the Mortgage Bankers Association, or MBA, is predicting a 53% decline in residential originations in 2004, we expect our total mortgage production to remain relatively constant during 2004 as compared to 2003. The decline in the MBA estimates is primarily due to an anticipated 58% decline in mortgage refinance activity. Our mortgage refinance share has been historically below the national average and was 51% during 2003 as compared to the MBA s estimated nationwide refinance share of 66%. Furthermore, our refinance share declined to 42% of total mortgage production during the fourth quarter of 2003 as compared to 54% during the third quarter of 2003 while total mortgage production increased 15% over the same period. Therefore, we believe that the decline in refinance activity is not likely to significantly affect our mortgage operations during 2004.

Other recent economic indicators, including increases in existing home sales, residential construction activity and mortgage applications, reinforce our expectation for 2004. In addition, as of December 31, 2003, the mortgage pipeline was $1.5 billion, of which $1.2 billion were ARMs and $337.6 million were FRMs. We expect that our ARM acquisitions and originations will be a higher percentage of total mortgage production than during 2003 and that less revenue from gain on sale of FRMs will be generated during 2004 than during 2003. However, we expect that the decline in revenue generated from gain on sale of loans, which we believe is more susceptible to short-term interest rate risk and can lead to volatility in the market value of mortgages in our mortgage pipeline, will be offset by cash flows and net earnings generated by our long-term mortgage portfolio. We believe that earnings generated by our long-term mortgage portfolio will generate a stream of revenue over a longer time horizon than would be realized from revenue generated from loan sales, which is also at risk if mortgage production were to decline from current levels.

It remains our goal to provide consistent and reliable dividends to our stockholders and, when appropriate, to increase our quarterly dividend to an amount that we believe is sustainable in the future. Therefore, during the fourth quarter of 2003, we increased our dividend 10% to $0.55 per share from the third quarter dividend of $0.50 per share. We believe that our business model, which includes centralized operating businesses

and a long-term mortgage portfolio, gives us more flexibility in generating consistent, reliable earnings and dividends. Our goal of providing consistent and reliable risk-adjusted returns that outperform the market during changing interest rate environments was successful in 2003. Particularly notable was the mortgage operations performance during the fourth quarter of 2003 which led to record acquisitions and originations. We are confident of future prospects for balance sheet and earnings growth as we believe momentum generated during the fourth quarter of 2003 positions us well for 2004.

Table of Contents

Results of Operations-For the Year Ended December 31, 2003 compared to the Year Ended December 31, 2002

Net earnings were $149.0 million, or $2.88 per diluted share, as compared to $40.3 million, or $0.99 per diluted share, for 2002. The year-over-year increase in net earnings of $108.7 million was primarily due to the following:

- $75.2 million increase in net interest income; and
- $34.5 million decrease in mark-to-market loss on derivatives.

These variances are discussed in further detail below.

Net Interest Income

We earn interest income primarily on mortgage assets which include CMO collateral, mortgages held-for-investment, mortgages held-for-sale, finance receivables and investment securities available-for-sale, or collectively, mortgage assets, and, to a lesser extent, interest income earned on cash and cash equivalents and due from affiliates. Interest expense is primarily interest paid on borrowings on mortgage assets, which include CMO borrowings, reverse repurchase agreements and borrowings on investment securities available-for-sale, and, to a lesser extent, interest expense paid on due to affiliates and senior subordinated debt. In our restated financial statements, net cash received or paid on derivatives is not a component of net interest income on the consolidated financial statements and, therefore, has no affect on the calculation of net interest spread or net interest margin. Net cash received or paid on derivatives is a component of mark-to-market gain (loss) derivative instruments on the consolidated financial statements.

Table of Contents

Comparative Yield Table. The following table summarizes average balance, interest and weighted average yield on mortgage assets and borrowings on mortgage assets for the periods indicated (dollars in thousands):

	For the year ended December 31,								
	2003			2002			2001		
	Average Balance	Interest	Yield	Average Balance	Interest	Yield	Average Balance	Interest	Yield
MORTGAGE ASSETS									
Subordinated securities collateralized by mortgages	$ 20,404	$ 3,515	17.23%	$ 28,931	$ 1,538	5.32%	$ 34,199	$ 3,517	10.28%
Mortgages held as CMO collateral (1)	6,620,328	318,459	4.81%	3,383,666	200,742	5.93%	1,508,208	112,624	7.47%
Mortgages held-for-investment and held-for-sale (2)	632,538	34,580	5.47%	114,519	6,781	5.92%	137,130	8,702	6.35%
Finance receivables (3)	604,087	28,969	4.80%	341,543	19,383	5.68%	205,474	15,556	7.57%
Total mortgage assets	$ 7,877,357	$ 385,523	4.89%	$ 3,868,659	$ 228,444	5.90%	$ 1,885,011	$ 140,399	7.45%
BORROWINGS									
CMO borrowings	$ 6,474,391	$ 174,199	2.69%	$ 3,298,934	$ 102,366	3.10%	$ 1,432,539	$ 74,235	5.18%
Reverse repurchase agreement	1,374,884	32,382	2.36%	814,248	23,583	2.90%	580,605	30,829	5.31%
Borrowings secured by investment securities (4)	2,709	2,316	85.49%	10,037	1,852	18.45%	17,199	2,566	14.92%
Total borrowings on mortgage assets	$ 7,851,984	$ 208,897	2.66%	$ 4,123,219	$ 127,801	3.10%	$ 2,030,343	$ 107,630	5.30%
Net Interest Spread (5)			2.23%			2.80%			2.15%
Net Interest Margin (6)			2.24%			2.60%			1.74%
Net Cash Payments on Derivatives (7)		$ 47,846			$ 28,361			$ 5,214	
Net Interest Margin including Net Cash Payments on Derivatives (8)			1.63%			1.87%			1.46%

(1) Interest includes $42.9 million, $23.2 million and $8.4 million, respectively, of amortization of acquisition cost on mortgages acquired from the mortgage operations. Interest also includes $21.1 million, $11.5 million and $3.2 million, respectively, of accretion of loan discounts, which represents the amount allocated to MSRs when they are sold to third parties and mortgages are transferred from the mortgage operations to the long-term investment operations and retained for long-term investment.

(2) Includes mortgages held-for-sale which were acquired via the consolidation of Impac Funding Corporation on July 1, 2003.

(3)

Total average borrowings on mortgage assets exceed total average mortgage assets during 2002 and 2001as we eliminated warehouse borrowings between the warehouse lending operations and mortgage operations prior to July 1, 2003 as part of the accounting restatements.

(4) Payments and excess cash flows received from investment securities collateralizing these borrowings were used to pay down the outstanding borrowings. The payments were received from a collateral base that was in excess of the borrowings. Therefore, while the payment amounts remained relatively stable, the average balance of the borrowings continued to decline. These borrowings were paid off during the third quarter of 2003 and the yield for 2003 reflects discount and securitization costs that were recorded as interest expense upon repayment of the borrowings.

(5) Net interest spread is calculated by subtracting the weighted average yield on total borrowings on mortgage assets from the weighted average yield on total mortgage assets.

(6) Net interest margin is calculated by subtracting interest expense on total borrowings on mortgage assets from interest income on total mortgage assets and then dividing by total average mortgage assets.

(7) Represents net cash paid on derivatives, which is a component of mark-to-market loss derivative instruments on the consolidated financial statements.

(8) Net interest margin including net cash payments on derivatives is calculated by subtracting interest expense on total borrowings on mortgage assets and net cash payments on derivatives from interest income on total mortgage assets and then dividing by total average mortgage assets.

Net interest income increased $75.2 million to $177.7 million for 2003 as compared to $102.5 million for 2002. The year-over-year increase in net interest income was primarily due to an increase in average mortgage assets, which increased to $7.9 billion for 2003 as compared to $3.9 billion for 2002 as the long-term investment operations retained $5.8 billion of primarily Alt-A mortgages acquired and originated by the mortgage operations and originated $290.5 million of multi-family mortgages.

Table of Contents

The increase in net interest income was partially offset by a decrease in net interest margins on mortgage assets which declined 36 basis points to 2.24% during 2003 as compared to 2.60% during 2002. The decrease in net interest margins on mortgage assets was primarily due interest rate adjustments on mortgage assets as follows:

at the time mortgages are retained for long-term investment, ARMs have initial coupons above the fully-indexed rate, which is the margin on the mortgage plus the index. Upon the mortgage interest rate reset date, interest rates on ARMs adjust downward to the fully-indexed rate. The reset to lower coupons on these mortgages during low interest rate environments, which was the case during 2003, is consistent with our strategy to mitigate the borrower s propensity to refinance their mortgage, which we believe will extend the duration of the mortgages;

hybrid ARMs acquired for long-term investment during 2001 with initial fixed interest rate periods of two years subsequently converted to ARMs, which resulted in those mortgages resetting to lower current interest rates during 2003; and

the decline in interest rates during 2003 led to record refinancing activity, which in turn led to increased mortgage prepayments and resulted in mortgages with coupons above current market interest rates were repaid and replaced with mortgages at lower yielding current market rates.

In addition, net interest margins on mortgage assets are susceptible to changes in interest rates due to mismatched interest rate adjustments between mortgage assets and borrowings on mortgage assets as follows:

interest rate adjustment limitations on mortgages held for long-term investment due to periodic and lifetime interest rate cap features as compared to borrowings which are not subject to adjustment limitations; and

mismatched interest rate adjustment periods between mortgages held for long-term investment and CMO borrowings.

Our interest rate risk management policies are formulated with the intent to offset the potential adverse effects of changing interest rates on cash flows on adjustable rate CMO borrowings. However, as a result of the combination of the factors listed above, the interest rate spread differential between ARMs and adjustable rate CMO borrowings compressed, which compressed net interest margins on mortgage assets. Net margin compression on mortgage assets was partially offset by a steep yield curve during 2003, which further steepened during the second half of 2003. A steep yield curve generally benefits net interest margins on our mortgage assets as coupons on mortgages are based, to some extent, on yields at the long end of the yield curve while our borrowing costs are indexed to yields at the short end of the yield curve, primarily one-month LIBOR.

The 36 basis point decline in net interest margins on mortgage assets was partially offset by the consolidation of the mortgage operations , see Restatement of Consolidated Financial Statements referenced above. The consolidation of the mortgage operations resulted in an 18 basis point increase in net interest margins on mortgage assets during 2003 as mortgages held-for-sale were consolidated with total average mortgage assets during the second half of 2003. During 2004 mortgages held-for-sale were not consolidated with total average mortgage assets as IFC was a non-consolidated entity prior to July 1, 2003. In addition, net interest margins on mortgages held-for-sale were favorable during 2003 due to a steep yield curve as compared to 2002. The yield curve represents the mathematical difference between short-term interest rates and long-term interest rates. Because the mortgage operations establishes interest rates on its mortgages by indexing those interest rates to long-term market interest rates and finances mortgages with borrowings that are indexed to short-term interest rates, a steep yield curve benefits net interest margins.

Mark-to-Market Loss Derivative Instruments

During 2003 mark-to-market loss on derivative instruments decreased to $16.0 million as compared to $50.2 million for 2002. The decrease in mark-to-market loss on derivative instruments was the result of changes in future expectations of short term rates which affected the value of our derivatives. We enter into derivative contracts to manage the various risks associated with certain specific liabilities. On the date we enter into various derivative contracts, the derivatives were designated as an economic hedge of the variability in expected future cash flows associated with a financing obligation or future liability. In our consolidated financial statements, we now record a market valuation adjustment for economic hedges and any subsequent cash payments paid or received on these derivatives as a current period expense or revenue in mark-to-market loss derivative instruments on the consolidated financial statements. In addition, we account for certain forward purchase commitments on mortgage loans as free-standing derivatives, and record the change in fair value of such instruments and the related derivatives used to hedge the mortgage pipeline as a current period expense or revenue.

Table of Contents

Results of Operations by Business Segment

We operate three core businesses:

- the long-term investment operations;
- the mortgage operations; and
- the warehouse lending operations.

Long-Term Investment Operations. Net earnings from the long-term operations was $105.4 million for 2003 as compared to $17.2 million for 2002. The increase in net earnings of $88.2 million was primarily due to a decrease in mark-to-market loss derivative instruments and an increase in net interest income. Mark-to-market loss derivative instruments declined by $41.4 million to a loss of $9.1 million for 2003 as compared to a loss of $50.5 million for 2002. Mark-to-market loss derivative instruments declined as future expectations of short-term rates positively affected the value of derivatives. Net interest income rose by $39.4 million to $130.5 million for 2003 as compared to $91.1 million for 2002 primarily due to an increase in total average mortgage assets. The long-term investment operations retained $6.1 billion of Alt-A and multi-family mortgages during 2003 which in turn led to an increase in average CMO collateral and mortgages held-for-investment as shown in the comparative yield table above. Refer to Note I. Segment Reporting in the notes to consolidated financial statements for additional detail. See Item 1. Business Long-Term Investment Operations and Note I. Segment Reporting in the notes to consolidated financial statements for additional detail regarding the operating structure and financial results of the long-term investment operations.

Mortgage Operations. Net earnings from the mortgage operations include its results of operations for the consolidation period on a consolidated basis. See Consolidation of IFC above. Prior to the consolidation of IFC, its results of operations were included in equity in net earnings of IFC on the consolidated financial statements. Equity in net earnings of IFC is reflected in Inter-company for purposes of segment reporting as shown in Note I. Segment Reporting in the notes to consolidated financial statements. As such, net earnings from the mortgage operations was $16.2 million during the consolidation period while equity in net earnings of IFC during the non-consolidation period was $11.5 million for 2003 as compared to $11.3 million for 2002. Net earnings from the mortgage operations were primarily earned from the sale of mortgage loans and the corresponding gains from the sale of those loans. Gain on sale of loans includes the difference between the price at which we acquire or originate mortgages and the price we receive upon the sale or securitization of mortgages plus or minus direct mortgage origination revenue and costs, i.e. loan and underwriting fees, commissions, appraisal review fees, document expense, etc. Gain on sale of loans acquired or originated by the mortgage operations also includes a premium for the sale of mortgage servicing rights upon the sale or securitization of mortgages, including REMICs and CMOs. Substantially all mortgages sold or securitized during 2003 were done so on a servicing released basis, which resulted in substantially all cash gains. In order to minimize risks associated with the accumulation of our mortgages, we seek to securitize or sell mortgages monthly by creating smaller transactions, thereby reducing our exposure to interest rate risk and price volatility during the accumulation period of mortgages. See Item 1. Business Mortgage Operations and Note I. Segment Reporting in the notes to consolidated financial statements for additional detail regarding the operating structure and financial results of the mortgage operations.

Warehouse Lending Operations. Net earnings from the warehouse lending operations was $27.5 million for 2003 as compared to $18.5 million for 2002. The increase in net earnings of $9.0 million was primarily due to an increase in net interest income. Net interest income rose during 2003 as total average finance receivables rose 77% to $604.1 million as compared to $341.5 million during 2002 as shown in the comparative yield table above. See Item 1. Business Warehouse Lending Operations and Note I. Segment Reporting in the notes to consolidated financial statements for additional detail regarding the operating structure and financial results of the warehouse lending operations.

Results of Operations-For the Year Ended December 31, 2002 compared to the Year Ended December 31, 2001

Net earnings (loss) increased to $40.3 million, or $0.99 per diluted share, for 2002 as compared to $(2.2) million, or $(0.16) per diluted share, for 2001. The year-over-year increase in net earnings of $42.5 million was primarily due to the following:

$69.1 million increase in net interest income; and

$17.1 million increase in mark-to-market loss on derivative instruments.

These variances are discussed in further detail below.

Table of Contents

Net Interest Income

We earn interest income primarily on mortgage assets which include CMO collateral, mortgages held-for-investment, mortgages held-for-sale, finance receivables and investment securities available-for-sale, or collectively, mortgage assets, and, to a lesser extent, interest income earned on cash and cash equivalents and due from affiliates. Interest expense is primarily interest paid on borrowings on mortgage assets, which include CMO borrowings, reverse repurchase agreements and borrowings on investment securities available-for-sale, and, to a lesser extent, interest expense paid on due to affiliates and senior subordinated debt. In our consolidated financial statements, net cash received or paid on derivatives is not a component of net interest income on the consolidated financial statements and, therefore, has no affect on the calculation of net interest spread or net interest margin. Net cash received or paid on derivatives is a component of mark-to-market gain (loss) derivative instruments on the consolidated financial statements.

Net interest income increased $69.1 million to $102.5 million for 2002 as compared to $33.4 million for 2001. The year-over-year increase in net interest income was primarily due to an increase in average mortgage assets, which increased to $3.9 billion for 2002 as compared to $1.9 billion for 2001 as the long-term investment operations retained $3.9 billion of primarily Alt-A mortgages acquired and originated by the mortgage operations.

The increase in net interest income was also due to an increase in net interest margins on mortgage assets which rose 86 basis points to 2.60% for 2002 compared to 1.74% for 2001 (refer to the comparative yield table above) primarily due to the following:

- decline in short-term interest rates during 2002 which reduced borrowing costs as compared to fixed rate coupons on hybrid mortgages which did not adjust downward; and

- accretion of loan discounts recognized on sale of MSRs.

As short-term interest rates continued to decline during 2002, interest rates on adjustable rate CMO borrowings, which are primarily indexed to one-month LIBOR, declined more rapidly than coupons on adjustable rate mortgages which are subject to interest rate adjustment limitations. In addition, fixed rate coupons on hybrid mortgages did not adjust downward as the majority of hybrid mortgages held-for-investment during 2002 were within the initial fixed rate period. Net interest margins on mortgage assets are susceptible to changes in interest rates due to mismatched interest rate adjustments between mortgage assets and borrowings on mortgage assets as follows:

- interest rate adjustment limitations on mortgages held for long-term investment due to periodic and lifetime interest rate cap features as compared to borrowings which are not subject to adjustment limitations ; and

- mismatched interest rate adjustment periods between mortgages held for long-term investment and CMO borrowings.

Accretion of loan discounts recognized on sale of MSRs also contributed to an increase in net interest margins. Mortgage loan discounts resulted in a 13 basis point contribution to net interest margins on mortgage assets as mortgage loan discounts increased to $11.5 million for 2002 as compared to $3.2 million for 2001. Mortgage loan discounts result from the sale of mortgage servicing rights when the mortgage loans are retained. Such discount is measured using the relative fair value method to allocate the carrying value of the loan between the MSRs sold and the mortgage loans retained. The resulting discount is accreted into interest income as a yield adjustment on mortgage assets.

Mark-to-Market Loss Derivative Instruments

During 2002 mark-to-market loss on derivative instruments increased to $50.5 million as compared to $33.4 million for 2001. The increase in mark-to-market loss on derivative instruments was the result of changes in future expectations of short term rates which affected the value of our derivatives. We enter into derivative contracts to manage the various risks associated with certain specific liabilities. On the date we enter into various derivative contracts, the derivatives were designated as an economic hedge of the variability in expected future cash flows associated with a financing obligation or future liability. In our consolidated financial statements, we now record a market valuation adjustment for economic hedges and any subsequent cash payments paid or received on these derivatives as a current period expense or revenue in mark-to-market loss derivative instruments on the consolidated financial statements. In addition, the Company accounts for certain forward purchase commitments on mortgage loans as free-standing derivatives, and records the change in fair value of such instruments and the related derivatives used to hedge the mortgage pipeline as a current period expense or revenue.

Table of Contents

Results of Operations by Business Segment

Long-Term Investment Operations. Net earnings from the long-term operations was $17.2 million for 2002 as compared to a loss of $16.3 million for 2001. The increase in net earnings of $33.5 million was primarily due to an increase in net interest income. Net interest income rose by $52.9 million to $91.1 million for 2002 as compared to $38.3 million for 2001 primarily due to an increase in total average mortgage assets. The long-term investment operations retained $3.9 billion of Alt-A and multi-family mortgages during 2002 which in turn led to an increase in average CMO collateral and mortgages held-for-investment as shown in the comparative yield table above. Refer to Note I. Segment Reporting in the notes to consolidated financial statements for additional detail. See Item 1. Business Long-Term Investment Operations and Note I. Segment Reporting in the notes to consolidated financial statements for additional detail regarding the operating structure and financial results of the long-term investment operations.

Mortgage Operations. Prior to the consolidation of IFC, its results of operations were included in equity in net earnings of IFC on the consolidated financial statements. Equity in net earnings of IFC is reflected in Inter-company for purposes of segment reporting as shown in Note I. Segment Reporting in the notes to consolidated financial statements. As such, equity in net earnings of IFC during the non-consolidation period was $11.3 million for 2002 as compared to $19.5 million for 2001. Net earnings from the mortgage operations were primarily earned from the sale of mortgage loans and the corresponding gains from the sale of those loans. Gain on sale of loans includes the difference between the price at which we acquire or originate mortgages and the price we receive upon the sale or securitization of mortgages plus or minus direct mortgage origination revenue and costs, i.e. loan and underwriting fees, commissions, appraisal review fees, document expense, etc. Gain on sale of loans acquired and originated by the mortgage operations also includes a premium for the sale of mortgage servicing rights upon the sale or securitization of mortgages, including REMICs and CMOs. Substantially all mortgages sold or securitized during 2002 were done so on a servicing released basis, which resulted in substantially all cash gains. In order to minimize risks associated with the accumulation of our mortgages, we seek to securitize or sell mortgages monthly by creating smaller transactions, thereby reducing our exposure to interest rate risk and price volatility during the accumulation period of mortgages. See Item 1. Business Mortgage Operations and Note I. Segment Reporting in the notes to consolidated financial statements for additional detail regarding the operating structure and financial results of the mortgage operations.

Warehouse Lending Operations. Net earnings from the warehouse lending operations was $18.5 million for 2002 as compared to $10.5 million for 2001. The increase in net earnings of $8.0 million was primarily due to an increase in net interest income. Net interest income rose during 2002 as total average finance receivables rose 65% to $341.5 million as compared to $205.5 million during 2001 as shown in the comparative yield table above. See Item 1. Business Warehouse Lending Operations and Note I. Segment Reporting in the notes to consolidated financial statements for additional detail regarding the operating structure and financial results of the warehouse lending operations.

Financial Condition

Total assets grew 63% to $10.6 billion at year-end 2003 as compared to $6.5 billion at year-end 2002 as the long-term investment operations retained $5.8 billion of primarily Alt-A mortgages and originated $290.5 million of multi-family mortgages. The retention of primarily Alt-A mortgages increased the long-term mortgage portfolio to $9.3 billion at year-end 2003 as compared to $5.2 billion at year-end 2002. Strong mortgage demand and the need to finance that demand resulted in a 77% increase in average finance receivables to non-affiliated clients of $604.1 million for 2003 as compared to $341.5 million for 2002.

Table of Contents

The following table presents selected financial data for the periods indicated (dollars in thousands, except per share data):

	As of and for the year ended December 31,		
	2003	2002	2001
Book value per share	$ 8.39	$ 6.26	$ 6.12
Return on average assets	1.80%	0.92%	(0.10)%
Return on average equity	41.59%	16.22%	(1.15)%
Assets to equity ratio	22.35:1	23.07:1	14.50:1
Debt to equity ratio	21.28:1	21.85:1	13.39:1
Allowance for loan losses as a percentage of loans provided for	0.39%	0.46%	0.46%
Constant prepayment rate, or CPR, on mortgages held as CMO collateral	28%	25%	34%
Total non-performing assets	$ 140,369	$ 130,614	$ 69,273
Total non-performing assets to total assets	1.33%	2.00%	2.44%
Mortgages owned 60+ days delinquent	$ 175,313	$ 161,260	$ 82,956
60+ day delinquency of mortgages owned	1.79%	3.22%	3.86%

We believe that in order for us to generate positive cash flows and net earnings from our long-term mortgage portfolio we must successfully manage the following primary operational and market risks:

- credit risk;
- prepayment risk;
- liquidity risk; and
- interest rate risk.

Credit Risk. We manage credit risk by primarily retaining high credit quality Alt-A mortgages, adequately providing for loan losses and actively managing delinquencies and defaults. We believe that by improving the overall credit quality of our long-term mortgage portfolio we can consistently generate stable future cash flow and net earnings. During 2003, we retained primarily Alt-A mortgages with an original weighted average credit score of 698 and an original weighted average LTV ratio of 77%. Alt-A mortgages are primarily first lien mortgages made to borrowers whose credit is generally within typical Fannie Mae and Freddie Mac guidelines, but that have loan characteristics that make them non-conforming under those guidelines. We primarily acquire non-conforming A or A- credit quality mortgages, collectively, Alt-A mortgages. By year-end 2003, the original weighted average credit score of mortgages held as CMO collateral was 694 and the original weighted average LTV ratio was 79%. For additional information regarding the long-term mortgage portfolio refer to Item 1. Long-Term Mortgage Portfolio, Note C CMO Collateral and Note D Mortgages Held-for-Investment in the accompanying notes to the consolidated financial statements.

In addition to retaining mortgages acquired and originated by our mortgage operations, the long-term investment operations originated $290.5 million of multi-family mortgages through IMCC. IMCC was formed to primarily originate small balance, multi-family mortgages of high credit quality. IMCC primarily originates hybrid ARMs with balances generally ranging from $250,000 to $3.0 million. Multi-family mortgages provide greater asset diversification on our balance sheet as multi-family mortgages typically have longer lives than residential mortgages. All multi-family mortgages originated during 2003 had interest rate floors with prepayment penalty periods ranging from three to seven years.

Table of Contents

We believe that we have adequately provided for loan losses by maintaining a ratio of allowance for loan losses to loans provided for of 39 basis points as of December 31, 2003 as allowance for loan losses increased to $38.6 million. As a comparison, the following table summarizes annualized trailing 12-month and life-to-date loss rates on mortgages held as CMO collateral as of December 31, 2003 (dollars in thousands, annualized trailing 12-month and life-to-date loss rates in basis points of beginning period collateral balance):

Issue Date	Issue Name	Original Collateral Balance ($)	Current Collateral Balance ($)	Annualized Trailing 120-Mo Loss Rate	Life-to-Date Loss Rate
May 2001	Impac CMB Trust Series 2001-1	359,643	66,617	37	32
Aug 2001	Impac CMB Trust Series 2001-2	403,480	109,511	42	26
Oct 2001	Impac CMB Trust Series 2001-3	400,000	132,951	16	19
Dec 2001	Impac CMB Trust Series 2001-4	350,000	141,881	30	34
Feb 2002	Impac CMB Trust Series 2002-1	500,000	251,326	15	14
Apr 2002	Impac CMB Trust Series 2002-2	499,998	267,735	9	7
Jun 2002	Impac CMB Trust Series 2002-3	750,000	439,808	4	5
Aug 2002	Impac CMB Trust Series 2002-4	200,004	122,414	14	16

All mortgages securing CMOs issued after Impac CMB Trust Series 2002-4 are unseasoned mortgages and have not experienced material life-to-date losses as of December 31, 2003. Actual net loan losses on the long-term mortgage portfolio increased to $12.9 million for 2003 as compared to $4.9 million for 2002. Actual net loan losses increased during 2003 as mortgages retained for long-term investment during 2001 became seasoned mortgages during 2003 and experienced higher losses than during 2002. Our mortgages generally initially experience a period of low delinquency and loss rates which gradually increase as mortgages become seasoned.

We monitor our servicers and sub-servicers to make sure that they perform loss mitigation, foreclosure and collection functions according to our servicing guide. This includes an effective and aggressive collection effort in order to minimize mortgages from becoming non-performing assets. However, when resolving issues related to non-performing assets, including potential disposition, servicers and sub-servicers are required to take timely and aggressive action. Servicers and sub-servicers are required to determine payment collection under various circumstances, which will result in maximum financial benefit. This is accomplished by either working with the borrower to bring the mortgage current or by foreclosing and liquidating the property. We perform ongoing review of mortgages that display weaknesses and believe that we maintain adequate loss allowance on our mortgages. When a borrower fails to make required payments on a mortgage and does not cure the delinquency within 60 days, we generally record a notice of default and commence foreclosure proceedings. If the mortgage is not reinstated within the time permitted by law for reinstatement, the property may then be sold at a foreclosure sale. In foreclosure sales, we generally acquire title to the property. As of year-end 2003, mortgages that we owned included 1.79% of mortgages that were 60 days or more delinquent compared to 3.22% as of year-end 2002 and 3.86% as of year-end 2001.

The following table summarizes mortgages that we own, including mortgages held for long-term investment and mortgages held-for-sale, that were 60 or more days delinquent for the periods indicated (in thousands):

	As of December 31,		
	2003	2002	2001
60-89 days delinquent	$ 51,173	$ 41,762	$ 21,820
90 or more days delinquent	52,080	33,822	21,416
Foreclosures	66,767	74,597	32,979

Delinquent bankruptcies	5,293	11,079	6,741
Total 60 or more days delinquent	$ 175,313	$ 161,260	$ 82,956

Non-performing assets consist of mortgages that are 90 days or more delinquent, or non-accrual loans, including loans in foreclosure and delinquent bankruptcies. It is our policy to place a mortgage on non-accrual status when it becomes 90 days delinquent. Any previously accrued interest will be reversed from revenue. When real estate is acquired in settlement of loans, or other real estate owned, the mortgage is written-down to a percentage of the property s appraised value or broker s price opinion. As of year-end 2003, non-performing assets as a percentage of total assets was 1.33% compared to 2.00% as of year-end 2002 and 2.44% as of year-end 2001.

The following table summarizes mortgages that we own, including mortgages held for long-term investment and mortgages held-for-sale, that were non-performing for the periods indicated (in thousands):

	As of December 31,		
	2003	**2002**	**2001**
Non-accrual	$ 124,140	$ 119,498	$ 61,136
Other real estate owned	16,229	11,116	8,137
Total non-performing assets	$ 140,369	$ 130,614	$ 69,273

Prepayment Risk. 79% of Alt-A mortgages retained in 2003 had prepayment penalty features ranging from two to seven years and at year-end 2003 81% of mortgages held as CMO collateral had active prepayment penalties. For 2003, the CPR of mortgages held as CMO collateral was 28% compared to 25% CPR for 2002 and 34% CPR for 2001, all of which we believe are below industry prepayment rates for those periods.

Liquidity Risk. We employ a leveraging strategy to increase assets by financing our long-term mortgage portfolio primarily with CMO borrowings, reverse repurchase agreements and capital and then using cash proceeds to acquire additional mortgage assets. We retain ARMs and FRMs that are acquired and originated from the mortgage operations and finance the acquisition of those mortgages, during this accumulation period, with reverse repurchase agreements. After accumulating a pool of mortgages, generally between $200 million and $1.0 billion, we securitize the mortgages in the form of CMOs. Our strategy is to securitize our mortgages every 15 to 45 days in order to reduce the accumulation period that mortgages are outstanding on short-term warehouse or reverse repurchase facilities, which reduces our exposure to margin calls on these facilities. CMOs are classes of bonds that are sold to investors in mortgage-backed securities and as such are not subject to margin calls. In addition, CMOs generally require a smaller initial cash investment as a percentage of mortgages financed than does interim warehouse and reverse repurchase financing. For additional information regarding financing refer to Item 1. Financing.

Because of the historically favorable prepayment and loss rates of our Alt-A mortgages, we have received favorable credit ratings on our CMOs from credit rating agencies, which has reduced our required initial capital investment. The ratio of total assets to total equity, or leverage ratio, was 22.35 to 1 at year-end 2003 compared to 23.07 to 1 at year-end 2002. This use of leverage at these historical levels allows us to grow our balance sheet by efficiently using available capital. We continually monitor our leverage ratio and liquidity levels to insure that we are adequately protected against adverse changes in market conditions. For additional information regarding liquidity refer to Liquidity and Capital Resources.

Interest Rate Risk. Refer to Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

Liquidity and Capital Resources

We recognize the need to have funds available for our operating businesses and our customer s demands for obtaining short-term warehouse financing until the settlement or sale of mortgages with us or with other investors. It is our policy to have adequate liquidity at all times to cover normal cyclical swings in funding availability and mortgage demand and to allow us to meet abnormal and unexpected funding requirements. We plan to meet liquidity through normal operations with the goal of avoiding unplanned sales of assets or emergency borrowing of funds. Toward this goal, ALCO is responsible for monitoring our liquidity position and funding needs.

ALCO is comprised of senior executives of the mortgage operations and warehouse lending operations. ALCO meets on a weekly basis to review current and projected sources and uses of funds. ALCO monitors the composition of the balance sheet for changes in the liquidity of our assets. Our primary liquidity consists of cash and cash equivalents and maturing mortgages, or liquid assets.

We believe that current cash balances, currently available financing facilities, capital raising capabilities and excess cash flows generated from our long-term mortgage portfolio will adequately provide for projected funding needs and asset growth. However, if we are unable to raise capital in the future, we may not be able to grow as planned. Refer to Item 1. Business Risk Factors for additional information regarding risks that could adversely affect our liquidity.

Our operating businesses primarily use available funds as follows:

- acquisition and origination of mortgages,
- investment in mortgages;
- provide short-term warehouse advances to affiliates and non-affiliates; and
- pay common stock dividends.

Acquisition and origination of mortgages. During 2003, the mortgage operations acquired $9.5 billion of primarily Alt-A mortgages, of which $5.8 billion was retained for long-term investment. Capital invested in mortgages is outstanding until we sell or securitize mortgages, which is one of the reasons we attempt to sell or securitize mortgages frequently. Initial capital

invested in mortgages includes premiums paid when mortgages are acquired and originated and initial capital investment, or haircut, required upon financing, which is generally determined by the type of collateral provided. The mortgage operations paid weighted average premiums of 1.86% on the principal balance of Alt-A mortgages acquired during 2003, which were financed with warehouse borrowings at a haircut generally between 2% to 5% of the outstanding principal balance of the mortgages.

When we finance mortgages with long-term CMO borrowings, we repay short-term warehouse financing and recoup our 2% to 5% haircut. Then, depending on credit ratings from national credit rating agencies on our CMOs, we are generally required to provide an initial capital investment of 0.50% to 1% of the principal balance of mortgages securing CMO financing. Therefore, our total capital investment in CMOs range from approximately 3% to 5% of the principal balance of mortgages, depending on premiums paid upon acquisition of mortgages, costs paid for completion of CMOs, costs to acquire derivatives and initial capital investment in CMOs required to achieve desired credit ratings.

In addition, the long-term investment operations originated $290.5 million of multi-family mortgages which were initially financed with short-term warehouse financing that generally require a 10% to 15% haircut. Multi-family mortgages are either sold as whole loan sales or are financed with CMO borrowings at lower haircut requirements than warehouse financing.

Provide short-term warehouse advances to affiliates and non-affiliates. We utilize uncommitted warehouse facilities with various lenders to provide short-term warehouse financing to affiliates and non-affiliated clients of the warehouse lending operations.

The warehouse lending operations provides short-term financing to non-affiliated clients from the closing of mortgages to their sale or other settlement with investors, including the mortgage operations. The warehouse lending operations generally finances between 95% and 98% of the fair market value of mortgages, which equates to a haircut requirement of between 2% and 5%, at prime rate plus a spread. At year-end 2003, the warehouse lending operations had $1.0 billion of approved warehouse lines available to non-affiliated clients, of which $630.0 million was outstanding.

The mortgage operations has uncommitted warehouse line agreements to obtain financing of up to $985.0 million from the warehouse lending operations at prime minus 0.50% during the period that the mortgage operations accumulates mortgages until the mortgages are securitized or sold. At December 31, 2003, the warehouse lending operations had $631.9 million in outstanding warehouse advances to the mortgage operations.

Our ability to meet liquidity requirements and the financing needs of our customers is subject to the renewal of our credit and repurchase facilities or obtaining other sources of financing, if required, including additional debt or equity from time to time. Any decision our lenders or investors make to provide available financing to us in the future will depend upon a number of factors, including:

- our compliance with the terms of our existing credit arrangements;
- our financial performance;
- industry and market trends in our various businesses;

the general availability of and rates applicable to financing and investments;

our lenders or investors resources and policies concerning loans and investments; and

the relative attractiveness of alternative investment or lending opportunities.

Pay common stock dividends. We paid common stock dividends of $127.8 million in 2003, which we generated from our operating activities. We are required to distribute a minimum of 90% of our taxable income to our stockholders in order to maintain our REIT status. Because we pay dividends based on taxable income, dividends may be more or less than net earnings. We paid total regular cash dividends of $2.53 per share in 2003 which met taxable income distribution requirements for the year.

Because the mortgage operations is seeking to retain earnings to fund the future growth of our mortgage operations business, the board of directors may decide that the mortgage operations should cease making dividend distributions in the

future. This would materially reduce the amount of our taxable income and in turn, would reduce the amount we would be required to distribute as dividends.

For additional information regarding dividend distribution requirements refer to Item 5. Market for Registrant s Common Equity and Related Stockholder Matters and Note A Summary of Business and Significant Accounting Policies in the accompanying notes to the consolidated financial statements.

Our operating businesses are primarily funded as follows:

- CMO borrowings and reverse repurchase agreements;
- excess cash flows from our long-term mortgage portfolio;
- sale and securitization of mortgages; and
- cash proceeds from the issuance of securities.

CMO borrowings and reverse repurchase agreements. We use CMO borrowings and reverse repurchase agreements to fund substantially all of our warehouse financing to affiliates and non-affiliated clients and the acquisition and origination of mortgages. As we accumulate mortgages, we finance the acquisition of mortgages primarily through borrowings on reverse repurchase agreements with third party lenders. We primarily use uncommitted repurchase facilities with major investment banks to finance substantially all warehouse financing, as needed. During 2003, we added an additional $750.0 million of new uncommitted warehouse facilities to finance asset growth. The new warehouse facilities provide us with a higher aggregate credit limit to fund the acquisition and origination of mortgages at terms comparable to those we have received in the past. These reverse repurchase agreements may have certain covenant tests which we continue to satisfy. As of December 31, 2003, the warehouse lending operations had $1.7 billion of uncommitted repurchase facilities with various lenders of which $1.6 billion was outstanding. Of total repurchase facilities, one of our lenders provides financing up to $125.0 million to finance the origination of multi-family mortgages.

From time to time during 2003, we utilized term repurchase financing provided to us by an underwriter of some of our securitizations at interest rates similar to our other repurchase facilities. These transactions allow us to reduce our borrowing costs relative to mortgages allocated to securitization transactions during the period immediately prior to the settlement of the securitization.

We expect to continue to use short-term warehouse facilities to fund the acquisition of mortgages. If we cannot renew or replace maturing borrowings, we may have to sell, on a whole loan basis, the mortgages securing these facilities, which, depending upon market conditions, may result in substantial losses. Additionally, if for any reason the market value of our mortgages securing warehouse facilities decline, our lenders may require us to provide them with additional equity or collateral to secure our borrowings, which may require us to sell mortgages at substantial losses.

In order to mitigate the liquidity risk associated with reverse repurchase agreements, we attempt to sell or securitize our mortgages between 15 to 45 days from acquisition or origination. Although securitizing mortgages more frequently adds operating and securitization costs, we believe the added cost is offset as liquidity is provided more frequently with less interest rate and price volatility, as the accumulation and holding period

of mortgages is shortened. When we have accumulated a sufficient amount of mortgages, generally between $200 million and $1.0 billion, we issue CMOs and convert short-term advances under reverse repurchase agreements to long-term CMO borrowings. The use of CMO borrowings provides the following benefits:

- allows us to lock in our financing cost over the life of the mortgages securing the CMO borrowings; and

- eliminates margin calls on the borrowings that are converted from reverse repurchase agreements to CMO financing.

For 2003, we completed $6.0 billion of CMOs, of which $5.3 billion were adjustable rate CMOs and $656.8 million were fixed rate CMOs, to provide long-term financing for the retention of $5.8 billion of primarily Alt-A mortgages and the origination of $290.5 million of multi-family mortgages. Because of the credit profile, historical loss performance and prepayment characteristics of our Alt-A mortgages, we have been able to borrow a higher percentage against the principal balance of mortgages held as CMO collateral, which means that we have to provide less initial capital upon completion of CMOs. Capital investment in the CMOs is established at the time CMOs are issued at levels sufficient to achieve desired credit ratings on the securities from credit rating agencies. Total credit loss exposure is limited to the capital invested in the

Table of Contents

CMOs at any point in time. As of December 31, 2003, total capital invested in mortgages held as CMO collateral was $149.2 million, which includes capitalized premiums paid, capitalized costs incurred to complete CMO borrowings and the required initial capital investment in CMOs.

For additional information regarding reverse repurchase agreements and CMO borrowings refer to Item 1. Financing, Note G Reverse Repurchase Agreements and Note H CMO Borrowings in the accompanying notes to the consolidated financial statements.

Excess cash flows from our long-term mortgage portfolio. For 2003, mortgages held as CMO collateral, which primarily comprises the long-term mortgage portfolio, generated excess cash flows of $156.4 million as compared to $112.6 million for 2002 and $44.0 million for 2001. We receive excess cash flows on mortgages held as CMO collateral after distributions are made to investors in CMOs to the extent cash or other collateral required to maintain desired credit ratings on the CMOs is fulfilled. Excess cash flows represent the difference between principal and interest payments on the mortgages less the following:

- interest paid to bondholders;
- pro-rata early principal prepayments paid to bondholders;
- servicing fees paid to mortgage servicers and sub-servicers;
- premiums paid to mortgage insurers; and
- actual losses incurred upon disposition of real estate acquired in settlement of mortgages.

Sale and securitization of mortgages. When the mortgage operations accumulates a sufficient amount of mortgages, generally between $100 million and $300 million, it sells mortgages to the long-term investment operations or to third party investors as whole loan sales or securitizes the mortgages as REMICs.

The mortgage operations transferred $5.8 billion of mortgages to the long-term investment operations during 2003, sold $2.7 billion of mortgages as whole loan sales and sold $887.5 million was securitized as REMICs. The mortgage operations sold mortgage servicing rights on substantially all mortgages in 2003. The sale of mortgage servicing rights generated substantially all cash, which was used to acquire and originate additional mortgage assets.

In order to mitigate interest rate and market risk, the mortgage operations attempts to sell and securitize mortgages between 15 and 45 days from acquisition and origination. Since we rely significantly upon sales and securitizations to generate cash proceeds to repay borrowings and to create credit availability, any disruption in our ability to complete sales and securitizations may require us to utilize other sources of financing, which, if available at all, may be on unfavorable terms. In addition, delays in closing sales and securitizations of our mortgages increase our risk by exposing us to credit and interest rate risk for this extended period of time.

Cash proceeds from the issuance of securities. We raised $150.4 million in net proceeds from the issuance of 11.0 million new shares of common stock during 2003. In addition, in December 2003, we filed with the SEC a shelf registration statement that allows us to sell up to $500.0 million of securities, including common stock, preferred stock, debt securities and warrants. We raised $106.5 million in net proceeds from the issuance of 5,750,000 new shares of common stock in February of 2004. By issuing new shares periodically throughout the year, we believe that we were able to utilize new capital more efficiently and profitably.

Pursuant to an equity distribution agreement with UBS Securities, LLC, we sold 904,300 shares of common stock and received net proceeds of approximately $14.4 million during the three months ended December 31, 2003. UBS Securities, LLC received a commission of 3% of the gross sales price per share of the shares of common stock sold pursuant to the equity distribution agreement, which amounted to an aggregate commission of $446,413 during the three months ended December 31, 2003.

Cash Flows

Operating Activities - Net cash provided by (used in) operating activities was $263.7 million for 2003 compared to $(188.3) million for 2002. Net earnings of $149.0 million during 2003 provided the majority of cash flows from operating

activities. Net cash provided by (used in) operating activities was $(188.3) million for 2002 compared to $156.8 million for 2001. The majority of cash flows used in operating activities during 2002 was primarily due to a reduction in advances to the mortgage operations.

Investing Activities - Net cash used in investing activities was $4.1 billion for 2003 compared to $3.3 billion for 2002. Net cash flows of $3.5 billion, including principal payments, was used in investing activities to acquire mortgages for long-term investment. Net cash used in investing activities was $3.3 billion for 2002 compared to $1.0 billion for 2001. Net cash flows of $3.0 billion, including principal payments, was used in investing activities to acquire mortgages for long-term investment.

Financing Activities - Net cash provided by financing activities was $3.8 billion for 2003 compared to $3.6 billion for 2002. Net cash flows of $3.4 billion provided by financing activities was primarily provided by CMO financing, net of principal repayments. Net cash provided by financing activities was $3.6 billion for 2002 compared to $896.6 million for 2002. Net cash flows of $2.8 billion provided by financing activities was primarily provided by CMO financing, net of principal repayments.

Inflation

The consolidated financial statements and corresponding notes to the consolidated financial statements 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 our operations. Unlike industrial companies, nearly all of our assets and liabilities are monetary in nature. As a result, interest rates have a greater impact on our performance than do the effects of general levels of inflation. Inflation affects our 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 mortgages 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 our yield and subsequently the value of our portfolio of mortgage assets.

Off-Balance Sheet Arrangements

On July 1, 2003, IMH acquired the assets and liabilities of IFC as IMH purchased 100% of the outstanding shares of voting common stock of IFC, which represents 1% of the economic interest in IFC. Prior to the July 1, 2003, IFC was a non-consolidating entity of IMH and was accounted for using the equity method of accounting by virtue of IMH s ownership of 100% of the outstanding non-voting preferred stock of IFC, which represents 99% of the economic interest in IFC. As a result of the acquisition, IMH began to consolidate IFC as of that date. We do not have any relationships with any unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. Refer to Item 7A. Quantitative and Qualitative Disclosures About Market Risk and Note O - Derivative Instruments in the accompanying notes to the consolidated financial statements for detail regarding off-balance sheet arrangements of consolidated entities.

Contractual Obligations

As of December 31, 2003, we had the following contractual obligations (in thousands):

	Payments Due by Period				
	Total	Less Than One Year	One to Three Years	Three to Five Years	More Than Five Years
CMO borrowings (1)	$ 8,526,838	$ 2,975,690	$ 3,346,809	$ 1,156,992	$ 1,047,347
Reverse repurchase agreements	1,568,807	1,568,807			
Operating leases	10,310	2,441	4,852	3,017	

(1) Reflects only the outstanding principal balance of CMOs outstanding during the period presented.

Payments on CMOs are dependent upon principal payments received from specific mortgages securing the CMO borrowings. These payments are determined using our estimates of future mortgage prepayment and loss rates of the underlying mortgages. If actual mortgage prepayment and loss rates differ from our estimates, the payment amounts will vary

Table of Contents

from the reported amounts. For additional information regarding our commitments refer to Note N Commitments and Contingencies in the accompanying notes to the consolidated financial statements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

General Overview

Although we manage credit, prepayment and liquidity risk in the normal course of business, we consider interest rate risk to be a significant market risk, which could potentially have the largest material impact on our financial condition and results of operations. Since a significant portion of our revenues and earnings are derived from net interest income, we strive to manage our interest-earning assets and interest-bearing liabilities to generate what we believe to be an appropriate contribution from net interest income. When interest rates fluctuate, profitability can be adversely affected by changes in the fair market value of our assets and liabilities and by the interest spread earned on interest-earning assets and interest-bearing liabilities. We derive income from the differential spread between interest earned on interest-earning assets and interest paid on interest-bearing liabilities. Any change in interest rates affects income received and income paid from assets and liabilities in varying and typically in unequal amounts. Changing interest rates may compress our interest rate margins and adversely affect overall earnings.

Interest rate risk management is the responsibility of ALCO, which reports results of interest rate risk analysis to the board of directors on a quarterly basis. ALCO establishes policies that monitor and coordinate sources, uses and pricing of 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. In addition, various modeling techniques are used to value interest sensitive mortgage-backed securities, including interest-only securities. The value of investment securities available-for-sale is determined using a discounted cash flow model using prepayment rate, discount rate and credit loss assumptions. Our investment securities portfolio is available-for-sale, which requires us to perform market valuations of the securities in order to properly record the portfolio. We continually monitor interest rates of our investment securities portfolio as compared to prevalent interest rates in the market. We do not currently maintain a securities trading portfolio and are not exposed to market risk as it relates to trading activities.

Changes in Interest Rates

ALCO follows interest rate risk management policies intended to limit our exposure to changes in interest rates primarily associated with cash flows on our adjustable rate CMO borrowings. Our primary objective is to limit our exposure to the variability in future cash flows attributable to the variability of one-month LIBOR, which is the underlying index of our adjustable rate CMO borrowings. We also monitor on an ongoing basis the prepayment risks that arise in fluctuating interest rate environments. Our interest rate risk management policies are formulated with the intent to offset the potential adverse effects of changing interest rates on cash flows on adjustable rate CMO borrowings.

We primarily acquire for long-term investment ARMs and hybrid ARMs and, to a lesser extent, FRMs. ARMs are generally subject to periodic and lifetime interest rate caps. This means that the interest rate of each ARM is limited to upwards or downwards movements on its periodic interest rate adjustment date, generally six months, or over the life of the mortgage. Periodic caps limit the maximum interest rate change, which can occur on any interest rate change date to generally a maximum of 1% per semiannual adjustment. Also, each ARM has a maximum lifetime interest rate cap. Generally, borrowings are not subject to the same periodic or lifetime interest rate limitations. During a period of rapidly increasing or decreasing interest rates, financing costs could increase or decrease at a faster rate than the periodic interest rate adjustments on mortgages would allow, which could affect net interest income. In addition, if market rates were to exceed the maximum interest rates of our ARMs, borrowing costs could increase while interest rates on ARMs would remain constant. We also acquire hybrid ARMs that have initial fixed interest rate periods generally ranging from two to seven years which subsequently convert to ARMs. During a rapidly increasing or decreasing interest rate environment financing costs would increase or decrease more rapidly than would interest rates on mortgages, which

would remain fixed until their next interest rate adjustment date. In order to provide some protection against any resulting basis risk shortfall on the related liabilities, we purchase derivatives. Derivatives are based upon the principal balance that would result under assumed prepayment speeds.

We measure the sensitivity of our net interest income to changes in interest rates affecting interest sensitive assets and liabilities using various simulations. These simulations take into consideration changes that may occur in investment and financing strategies, changes in the forward yield curve, changes in interest rate risk management strategies, changes in mortgage prepayment speeds and changes in the volume of mortgage acquisitions and originations.

Table of Contents

As part of various interest rate simulations, we calculate the effect of potential changes in interest rates on our interest-earning assets and interest-bearing liabilities and their affect on overall earnings. The simulations assume instantaneous and parallel shifts in interest rates and to what degree those shifts affect net interest income. First, we estimate net interest income along with net cash flows on derivatives for the next twelve months using balance sheet data and the notional amount of derivatives as of December 31, 2003 and 12-month projections of the following:

future interest rates using forward yield curves, which are market consensus estimates of future interest rates;

mortgage acquisition and originations;

mortgage prepayment rate assumptions; and

forward swap rates.

We refer to the 12-month projection of net interest income along with the 12-month projection of net cash flows on derivatives as the base case. For financial reporting purposes, net cash flows on derivative instruments are included in market-to-market loss derivative instruments on the consolidated financial statements. However, for purposes of interest rate risk analysis we include net cash flows on derivatives in our base care simulations as we acquire derivatives to offset the effect that changes in interest rates have on variable borrowing costs, such as CMO and warehouse borrowings. We believe that including net cash flows on derivatives in our interest rate risk analysis presents a more useful simulation of the effect of changing interest rates on net cash flows generated by our long-term mortgage portfolio. Once the base case has been established, we shock the base case with instantaneous and parallel shifts in interest rates in 100 basis point increments upward and downward. Calculations are made for each of the defined instantaneous and parallel shifts in interest rates over or under the forward yield curve used to determine the base case and including any associated changes in projected mortgage prepayment rates caused by changes in interest rates. The results of each 100 basis point change in interest rates are then compared against the base case to determine the estimated dollar and percentage change to base case. The simulations consider the affect of interest rate changes on interest sensitive assets and liabilities as well as derivatives. The simulations also consider the impact that instantaneous and parallel shift in interest rates have on prepayment rates and the resulting affect of accelerating or decelerating amortization of premium and securitization costs.

The following table estimates the financial impact to base case, including net cash flow from derivatives, from various instantaneous and parallel shifts in interest rates based on both our on- and off-balance sheet structure as of December 31, 2003 and 2002 (dollar amounts in millions). Our off-balance sheet structure refers to the notional amount of derivatives that are not recorded on our balance sheet. Since these estimates are based upon numerous assumptions, actual sensitivity to interest rate changes could vary if actual experience differs from the assumptions used.

	Changes in base case as of December 31, 2003 (1)				
	Base case, excluding net cash flow on derivatives		Net cash flow on derivatives	Base case, including net cash flow on derivatives	
Instantaneous and Parallel Change in Interest Rates (2)	**($)**	**(%)**	**($)**	**($)**	**(%)**
Up 300 basis points, or 3% (3)	(162.3)	(75)	182.6	20.3	12
Up 200 basis points, or 2%	(99.8)	(46)	121.7	21.9	13

Up 100 basis points, or 1%	(44.3)	(20)	60.9	16.6	10
Down 100 basis points, or 1%	57.3	26	60.7	(3.4)	(2)
Down 200 basis points, or 2% (4)	n/a	n/a	n/a	n/a	n/a

	Changes in base case as of December 31, 2002 (1)				
	Base case, excluding net cash flow on derivatives		**Net cash flow on derivatives**	**Base case, including net cash flow on derivatives**	
Instantaneous and Parallel Change in Interest Rates (2)	**($)**	**(%)**	**($)**	**($)**	**(%)**
Up 200 basis points, or 2%	(46.1)	(26)	38.2	(7.9)	(6)
Up 100 basis points, or 1%	(24.3)	(14)	19.4	(4.9)	(4)
Down 100 basis points, or 1%	27.9	16	(19.8)	8.1	6
Down 200 basis points, or 2% (4)	32.0	18	(22.0)	10.0	8