

IMPAC MORTGAGE HOLDINGS INC

Form 10-Q

November 08, 2016

Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2016

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)

Edgar Filing: IMPAC MORTGAGE HOLDINGS INC - Form 10-Q

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

19500 Jamboree Road, Irvine, California 92612

(Address of principal executive offices)

(949) 475-3600

(Registrant's telephone number, including area code)

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

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

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

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

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

There were 16,015,983 shares of common stock outstanding as of November 4, 2016.

Table of Contents

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

FORM 10-Q QUARTERLY REPORT

TABLE OF CONTENTS

	Page
 <u>PART I. FINANCIAL INFORMATION</u>	
 <u>ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS</u>	
<u>Consolidated Balance Sheets as of September 30, 2016 (unaudited) and December 31, 2015</u>	3
<u>Consolidated Statements of Operations for the Three and Nine Months Ended September 30, 2016 and 2015 (unaudited)</u>	4
<u>Consolidated Statement of Changes in Stockholders' Equity for the Nine Months Ended September 30, 2016 (unaudited)</u>	5
<u>Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2016 and 2015 (unaudited)</u>	6
<u>Notes to Unaudited Consolidated Financial Statements</u>	7
 <u>ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	
<u>Forward-Looking Statements</u>	36
<u>The Mortgage Industry and Discussion of Relevant Fiscal Periods</u>	36
<u>Selected Financial Results</u>	37
<u>Status of Operations</u>	37
<u>Liquidity and Capital Resources</u>	42
<u>Critical Accounting Policies</u>	44
<u>Financial Condition and Results of Operations</u>	45
 <u>ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	
 <u>ITEM 4. CONTROLS AND PROCEDURES</u>	
 <u>PART II. OTHER INFORMATION</u>	
 <u>ITEM 1. LEGAL PROCEEDINGS</u>	
 <u>ITEM RISK FACTORS</u>	
<u>1A.</u>	70
 <u>ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS</u>	
 <u>ITEM 3. DEFAULTS UPON SENIOR SECURITIES</u>	
 <u>ITEM 4. MINE SAFETY DISCLOSURES</u>	

<u>ITEM 5. OTHER INFORMATION</u>	70
<u>ITEM 6. EXHIBITS</u>	71
<u>SIGNATURES</u>	72
CERTIFICATIONS	

Table of Contents

PART I. FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)

	September 30, 2016 (Unaudited)	December 31, 2015
ASSETS		
Cash and cash equivalents	\$ 58,902	\$ 32,409
Restricted cash	9,928	3,474
Mortgage loans held-for-sale	849,521	310,191
Finance receivables	78,653	36,368
Mortgage servicing rights	87,413	36,425
Securitized mortgage trust assets	4,169,519	4,594,534
Goodwill	104,938	104,938
Intangible assets, net	26,827	29,975
Deferred tax asset, net	24,420	24,420
Other assets	49,712	38,118
Total assets	\$ 5,459,833	\$ 5,210,852
LIABILITIES		
Warehouse borrowings	\$ 880,111	\$ 325,616
Term financing	29,871	29,716
Convertible notes	24,962	44,819
Contingent consideration	59,896	48,079
Long-term debt	39,835	31,898
Securitized mortgage trust liabilities	4,151,389	4,580,326
Other liabilities	60,088	35,908
Total liabilities	5,246,152	5,096,362
Commitments and contingencies (See Note 14)		
STOCKHOLDERS' EQUITY		
Series A-1 junior participating preferred stock, \$0.01 par value; 2,500,000 shares authorized; none issued or outstanding	—	—
Series B 9.375% redeemable preferred stock, \$0.01 par value; liquidation value \$16,640; 2,000,000 shares authorized, 665,592 noncumulative shares issued and outstanding as of September 30, 2016 and December 31, 2015, respectively	7	7
Series C 9.125% redeemable preferred stock, \$0.01 par value; liquidation value \$35,127; 5,500,000 shares authorized; 1,405,086 noncumulative shares issued and outstanding as of September 30, 2016 and December 31, 2015, respectively	14	14

Edgar Filing: IMPAC MORTGAGE HOLDINGS INC - Form 10-Q

Common stock, \$0.01 par value; 200,000,000 shares authorized; 16,015,649 and 10,326,520 shares issued and outstanding as of September 30, 2016 and December 31, 2015, respectively	160	103
Additional paid-in capital	1,167,707	1,098,302
Net accumulated deficit:		
Cumulative dividends declared	(822,520)	(822,520)
Retained deficit	(131,687)	(161,416)
Net accumulated deficit	(954,207)	(983,936)
Total stockholders' equity	213,681	114,490
Total liabilities and stockholders' equity	\$ 5,459,833	\$ 5,210,852

See accompanying notes to unaudited consolidated financial statements

Table of Contents

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)

(Unaudited)

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2016	2015	September 30, 2016	2015
Revenues:				
Gain on sale of loans, net	\$ 113,158	\$ 47,274	\$ 245,849	\$ 133,018
Real estate services fees, net	2,678	2,775	6,773	7,872
Servicing income, net	3,789	2,432	8,680	4,083
Loss on mortgage servicing rights	(15,857)	(4,818)	(41,249)	(14,176)
Other	225	(11)	453	283
Total revenues	103,993	47,652	220,506	131,080
Expenses:				
Personnel expense	38,467	21,315	93,025	56,883
Business promotion	10,350	10,735	30,828	19,628
General, administrative and other	7,736	7,100	23,742	20,479
Accretion of contingent consideration	1,591	2,424	5,244	5,471
Change in fair value of contingent consideration	23,215	(16,897)	34,569	(28,223)
Total expenses	81,359	24,677	187,408	74,238
Operating income:	22,634	22,975	33,098	56,842
Other income (expense):				
Interest income	64,932	70,301	201,561	210,177
Interest expense	(63,628)	(70,182)	(199,525)	(208,042)
Change in fair value of long-term debt	(8,641)	—	(7,286)	(8,661)
Change in fair value of net trust assets, including trust				
REO gains (losses)	1,071	(3,004)	2,609	(3,078)
Total other expense	(6,266)	(2,885)	(2,641)	(9,604)
Earnings before income taxes	16,368	20,090	30,457	47,238
Income tax (benefit) expense	(130)	781	728	(22,852)
Net earnings	\$ 16,498	\$ 19,309	\$ 29,729	\$ 70,090
Earnings per common share :				
Basic	\$ 1.28	\$ 1.89	\$ 2.43	\$ 7.00
Diluted	1.18	1.48	2.27	5.61

See accompanying notes to unaudited consolidated financial statements

Table of Contents

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

(in thousands, except share amounts)

(Unaudited)

	Preferred Shares Outstanding	Preferred Stock	Common Shares Outstanding	Common Stock	Additional Paid-In Capital	Cumulative Dividends Declared	Retained Deficit	Total Stockholder Equity
Balance, December 31, 2015	2,070,678	\$ 21	10,326,520	\$ 103	\$ 1,098,302	\$ (822,520)	\$ (161,416)	\$ 114,490
Proceeds and tax benefit from exercise of stock options	—	—	38,620	1	209	—	—	210
Stock based compensation	—	—	—	—	1,647	—	—	1,647
Common stock issuance, net	—	—	3,811,429	38	47,567	—	—	47,605
Convertible note share issuance	—	—	1,839,080	18	19,982	—	—	20,000
Net earnings	—	—	—	—	—	—	29,729	29,729
Balance, September 30, 2016	2,070,678	\$ 21	16,015,649	\$ 160	\$ 1,167,707	\$ (822,520)	\$ (131,687)	\$ 213,681

See accompanying notes to unaudited consolidated financial statements

Table of Contents

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(Unaudited)

	For the Nine Months Ended September 30,	
	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net earnings	\$ 29,729	\$ 70,090
Loss on sale of mortgage servicing rights	10,610	6,193
Change in fair value of mortgage servicing rights	32,048	7,983
Gain on sale of mortgage loans	(212,696)	(115,578)
Change in fair value of mortgage loans held-for-sale	(19,572)	(9,030)
Change in fair value of derivatives lending, net	(14,618)	(8,755)
Provision for repurchases	778	340
Origination of mortgage loans held-for-sale	(9,813,665)	(7,319,723)
Sale and principal reduction on mortgage loans held-for-sale	9,414,794	7,146,796
Losses from REO	5,971	4,899
Change in fair value of net trust assets, excluding REO	(10,273)	(4,977)
Change in fair value of long-term debt	7,286	8,661
Accretion of interest income and expense	96,036	111,400
Amortization of intangible and other assets	3,577	2,384
Accretion of contingent consideration	5,244	5,471
Change in fair value of contingent consideration	34,569	(28,223)
Amortization of debt issuance costs and discount on note payable	398	248
Stock-based compensation	1,647	1,076
Impairment of deferred charge	815	1,054
Change in deferred tax assets	—	(24,420)
Change in REO impairment reserve	—	1,655
Net change in restricted cash	(6,454)	(3,409)
Net change in other assets and liabilities	18,687	8,647
Net cash used in operating activities	(415,089)	(137,218)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net change in securitized mortgage collateral	461,063	479,565
Proceeds from the sale of mortgage servicing rights	5,153	23,079
Finance receivable advances to customers	(672,885)	(523,005)
Repayments of finance receivables	630,600	490,029
Net change in mortgages held-for-investment	45	46
Purchase of premises and equipment	(147)	93
Net principal change on investment securities available-for-sale	47	83
Acquisition of CashCall Mortgage	—	(5,000)
Proceeds from the sale of REO	32,275	24,210
Net cash provided by investing activities	456,151	489,100
CASH FLOWS FROM FINANCING ACTIVITIES:		

Edgar Filing: IMPAC MORTGAGE HOLDINGS INC - Form 10-Q

Net proceeds from issuance of common stock	47,605	—
Issuance of convertible notes	—	25,000
Issuance of term financing	—	30,000
Repayment of warehouse borrowings	(8,988,778)	(6,884,047)
Borrowings under warehouse agreement	9,543,273	7,135,002
Repayment of line of credit	—	(11,000)
Borrowings under line of credit	—	7,000
Repayment of short-term borrowing	—	(15,000)
Short-term borrowing	—	15,000
Repayment of securitized mortgage borrowings	(588,390)	(614,505)
Payment of acquisition related contingent consideration	(27,996)	(32,423)
Principal payments on short-term debt	—	(6,000)
Principal payments on capital lease	(393)	(616)
Debt issuance costs	(100)	(500)
Proceeds from exercise of stock options	210	643
Net cash used in financing activities	(14,569)	(351,446)
Net change in cash and cash equivalents	26,493	436
Cash and cash equivalents at beginning of period	32,409	10,073
Cash and cash equivalents at end of period	\$ 58,902	\$ 10,509
NON-CASH TRANSACTIONS :		
Transfer of securitized mortgage collateral to real estate owned	\$ 32,719	\$ 30,307
Mortgage servicing rights retained from loan sales and issuance of mortgage backed securities	91,809	76,119
Common stock issued upon conversion of debt	20,000	—
Acquisition of equipment purchased through capital leases	551	413
Acquisition related goodwill asset related to CashCall	—	104,586
Acquisition related intangible assets related to CashCall	—	33,122
Acquisition related contingent consideration liability related to CashCall	—	124,592
Common stock issued related to CashCall acquisition	—	6,150

See accompanying notes to unaudited consolidated financial statements

Table of Contents

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

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

Note 1.—Summary of Business and Financial Statement Presentation

Business Summary

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

The Company's operations include the mortgage lending operations and real estate services conducted by IRES and IMC and the long-term mortgage portfolio (residual interests in securitizations reflected as net trust assets and liabilities in the consolidated balance sheets) conducted by IMH. Beginning in the first quarter of 2015, the mortgage lending operations include the activities of the CashCall Mortgage operations (CCM) (See Note 2. – Acquisition of CashCall Mortgage.)

Financial Statement Presentation

The accompanying unaudited consolidated financial statements of IMH and its subsidiaries (as defined above) have been prepared in accordance with Accounting Principles Generally Accepted in the United States of America (GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments, consisting of normal recurring adjustments considered necessary for a fair presentation, have been included. Operating results for the three months ended September 30, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016. These interim period condensed consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements, which are included in the Company's Annual Report on Form 10-K for the year ended December 31, 2015, filed with the United States Securities and Exchange Commission (SEC).

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

Management has made a number of material estimates and assumptions relating to the reporting of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period to prepare these consolidated financial statements in conformity with GAAP. Material estimates subject to change include the fair value estimates of assets acquired and liabilities assumed in the acquisition of CCM as discussed in Note 2. — Acquisition of CashCall Mortgage. Additionally, other items affected by such estimates and assumptions include the valuation of trust assets and trust liabilities, contingencies, the estimated obligation of repurchase liabilities related to sold loans, the valuation of long-term debt, mortgage servicing rights, mortgage loans held-for-sale and derivative instruments, including interest rate lock commitments (IRLC). Actual results could differ from those estimates and assumptions.

Recent Accounting Pronouncements

In April 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2015-03, “Interest—Imputation of Interest (Subtopic 835-30), Simplifying the Presentation of Debt Issuance Costs”, which requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability. For public business entities, the ASU is effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. Entities should apply the new guidance on a retrospective basis, wherein the balance sheet of each individual period presented should be adjusted to reflect the period-specific effects of applying the new guidance. Upon transition, entities are required to comply with the applicable disclosures for a change in an accounting principle. In August 2015, ASU

7

Table of Contents

2015-15, Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements, was issued to address ASU 2015-03 as it relates to line-of-credit arrangements. Given the absence of authoritative guidance within ASU 2015-03 for debt issuance costs related to line-of-credit arrangements, the SEC staff stated that it would not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the line of credit arrangement. We adopted this change retrospectively on January 1, 2016, which resulted in a \$465 thousand reclassification from other assets to Term Financing and Convertible Notes on December 31, 2015. The adoption of this ASU did not have a material impact on the Company's consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, "Improvements to Employee Share-Based Payment Accounting". ASU 2016-09 simplifies several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities and classification on the statement of cash flows. This ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016. Early adoption is permitted. The adoption of this ASU is not expected to have a material impact on the Company's consolidated financial statements.

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

Note 2.—Acquisition of CashCall Mortgage

On January 6, 2015, the Company entered into an Asset Purchase Agreement (the Asset Purchase Agreement) with CashCall, Inc. (CashCall), an unrelated entity, pursuant to which the Company agreed to purchase certain assets of CashCall's residential mortgage operations. Upon closing, which occurred on March 31, 2015, CashCall's mortgage operations began to operate as a separate division of IMC under the name CashCall Mortgage (CCM).

Pursuant to the Asset Purchase Agreement, and subject to the terms and conditions contained therein, the purchase price consists of a fixed component and a contingent component. The fixed component includes (i) the aggregate payment of \$10 million in cash, payable in installments through January 2016 and (ii) 494,017 newly issued unregistered shares of the Company. The contingent component consists of a three year earn-out provision beginning on the effective date (January 2, 2015) of 100% of pre-tax net earnings of CCM for January and February of 2015, 65% of the pre-tax net earnings for the next 10 months of 2015, 55% of pre-tax 2016 net earnings and 45% of pre-tax 2017 net earnings. During the three and nine months ended September 30, 2016, consideration paid to CashCall, Inc. was \$2.5 million pursuant to the fixed component of the Asset Purchase Agreement and \$14.9 million and \$28.0 million, respectively, pursuant to the earn-out provision.

If, during the four years following January 2, 2015, the Company sells all or substantially all of its assets or the assets of CCM, the division of IMC, or a person acquires 50% or more of the securities of the Company or IMC, then the Company will pay additional contingent consideration, subject to adjustment, to CashCall of 15% of the enterprise value (as defined in the Asset Purchase Agreement) in excess of \$200 million plus an additional 5% of the enterprise value in excess of \$500 million (Business Appreciation Rights).

Table of Contents

The table below presents the purchase price allocation of the estimated fair values of assets acquired and the liabilities assumed as of March 31, 2015.

Consideration paid:	
Cash	\$ 5,000
IMH common stock	6,150
Deferred payments	5,000
Contingent consideration (1)	124,592
	\$ 140,742
Assets acquired:	
Trademark	\$ 17,251
Customer list	10,170
Non-compete agreement	5,701
Fixed assets and software	3,034
Total assets acquired	36,156
Liabilities assumed:	
Total liabilities assumed	—
Goodwill	\$ 104,586

(1) Included within the contingent consideration is \$1.4 million of Business Appreciation Rights, as defined above. The CCM acquisition was accounted for under the acquisition method of accounting pursuant to FASB Accounting Standards Codification (ASC) 805, Business Combinations. The assets and liabilities, both tangible and intangible, were recorded at their estimated fair values as of the acquisition date. The Company made significant estimates and exercised significant judgment in estimating fair values of the acquired assets and assumed liabilities. The application of the acquisition method of accounting resulted in tax deductible goodwill of \$104.6 million. The acquisition closed on March 31, 2015; however, the effective date of the transaction was January 2, 2015. From the effective date to the date of the close, IMC was entitled to and recognized the net earnings of the loans originated by CCM. Acquisition related costs of \$0.3 million were expensed as incurred. The expenses were comprised primarily of legal and professional fees.

Unaudited Pro Forma Results of Operations

The following table presents unaudited pro forma results of operations as if the CCM acquisition had been completed on January 1, 2014. The unaudited pro forma results of operations include the historical accounts of the Company and CCM and pro forma adjustments, including the amortization of intangibles with definite lives, depreciation of fixed assets, accretion of discount on contingent consideration and elimination of commissions and loan due diligence costs of IMC. The unaudited pro forma information presented below is intended for informational purposes only and is not necessarily indicative of the future operating results or operating results that would have occurred had the CCM acquisition been completed at the beginning of 2014. No assumptions have been applied to the pro forma results of operations regarding possible revenue enhancements, expense efficiencies or asset dispositions.

	For the Three and Nine Months Ended September 30, 2015	
Revenues	\$ 47,652	\$ 149,480
Other expense	(2,885)	(9,394)
Expenses	(28,864)	(106,707)

Pretax net earnings \$ 15,903 \$ 33,379

Table of Contents

Note 3.—Mortgage Loans Held-for-Sale

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

	September 30, 2016	December 31, 2015
Government (1)	\$ 160,863	\$ 104,576
Conventional (2)	616,071	170,519
Other (3)	42,158	24,239
Fair value adjustment (4)	30,429	10,857
Total mortgage loans held for sale	\$ 849,521	\$ 310,191

(1) Includes all government-insured loans including Federal Housing Administration (FHA), Veterans Affairs (VA) and United States Department of Agriculture (USDA).

(2) Includes loans eligible for sale to Federal National Mortgage Association (Fannie Mae or FNMA) and Federal Home Loan Mortgage Corporation (Freddie Mac or FHLMC).

(3) Includes NonQM and Jumbo loans.

(4) Changes in fair value are included in the statements of operations.

Gain on mortgage loans held-for-sale (LHFS), included in gain on sale of loans, net in the consolidated statement of operations, is comprised of the following for the three and nine months ended September 30, 2016 and 2015:

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2016	2015	September 30, 2016	2015
Gain on sale of mortgage loans	\$ 109,059	\$ 59,753	\$ 252,084	\$ 179,894
Premium from servicing retained loan sales	40,890	23,384	91,809	76,119
Unrealized gains from derivative financial instruments	5,836	955	14,294	8,754
Realized losses from derivative financial instruments	(3,098)	(6,747)	(18,687)	(8,453)
Mark to market gain on LHFS	5,300	6,678	19,572	9,030
Direct origination expenses, net	(44,902)	(37,729)	(112,445)	(131,986)
Recovery (provision) for repurchases	73	980	(778)	(340)
Total gain on sale of loans, net	\$ 113,158	\$ 47,274	\$ 245,849	\$ 133,018

Note 4.—Mortgage Servicing Rights

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

interest, tax and insurance payments.

10

Table of Contents

The following table summarizes the activity of MSR's for the nine months ended September 30, 2016 and year ended December 31, 2015:

	September 30, 2016	December 31, 2015
Balance at beginning of period	\$ 36,425	\$ 24,418
Additions from servicing retained loan sales	91,809	98,103
Reductions from bulk sales	(8,773)	(75,157)
Changes in fair value (1)	(32,048)	(10,939)
Fair value of MSR's at end of period	\$ 87,413	\$ 36,425

(1) Changes in fair value are included within loss on mortgage servicing rights in the consolidated statements of operations.

At September 30, 2016 and December 31, 2015, the outstanding principal balance of the mortgage servicing portfolio was comprised of the following:

	September 30, 2016	December 31, 2015
Government insured (1)	\$ 948,532	\$ 675,744
Conventional (2)	8,311,402	2,799,758
NonQM	190,760	95,157
Total loans serviced	\$ 9,450,694	\$ 3,570,659

(1) As of September 30, 2016, the Government insured servicing rights have been pledged as collateral as part of the Term Financing. (See Note 7. — Term Financing.)

(2) As of September 30, 2016, the Conventional servicing rights have been pledged as collateral and subject to acknowledgement agreements with FNMA and FHLMC as part of the Term Financing. (See Note 7. — Term Financing.)

The table below illustrates hypothetical changes in fair values of MSR's, caused by assumed immediate changes to key assumptions that are used to determine fair value. See Note 10.—Fair Value of Financial Instruments for a description of the key assumptions used to determine the fair value of MSR's.

	September 30, 2016
Mortgage Servicing Rights Sensitivity Analysis	
Fair value of MSR's	\$ 87,413
Prepayment Speed:	
Decrease in fair value from 10% adverse change	(3,785)
Decrease in fair value from 20% adverse change	(7,289)
Decrease in fair value from 30% adverse change	(10,536)
Discount Rate:	
Decrease in fair value from 10% adverse change	(3,009)

Edgar Filing: IMPAC MORTGAGE HOLDINGS INC - Form 10-Q

Decrease in fair value from 20% adverse change	(5,820)
Decrease in fair value from 30% adverse change	(8,452)

Sensitivities are hypothetical changes in fair value and cannot be extrapolated because the relationship of changes in assumptions to changes in fair value may not be linear. Also, the effect of a variation in a particular assumption is calculated without changing any other assumption, whereas a change in one factor may result in changes

Table of Contents

to another. Accordingly, no assurance can be given that actual results would be consistent with the results of these estimates. As a result, actual future changes in MSR values may differ significantly from those displayed above.

Loss on mortgage servicing rights is comprised of the following for the three and nine months ended September 30, 2016 and 2015:

	For the Three Months Ended September 30, 2016		For the Nine Months Ended September 30, 2015	
Change in fair value of mortgage servicing rights	\$ (8,224)	\$ (4,347)	\$ (32,048)	\$ (7,983)
Loss on sale of mortgage servicing rights	(7,532)	(471)	(10,610)	(6,193)
Realized and unrealized (losses) gains from hedging instruments	(101)	—	1,409	—
Loss on mortgage servicing rights	\$ (15,857)	\$ (4,818)	\$ (41,249)	\$ (14,176)

In the third quarter of 2016, the Company recorded \$8.2 million in change in fair value of mortgage servicing rights, including \$9.4 million in MSR MTM losses due to prepayments offset by a MTM gain at September 30, 2016 of \$1.2 million, as a result of a slight increase in rates during September.

During the third quarter of 2016, the Company entered into an agreement to modify previous MSR sales agreements for three loan pools with a certain investor whereby such investor would allow the Company to solicit borrowers in the previously sold loan pools. Under the agreement, the Company agreed to extend the prepayment protection terms and to reimburse the investor up to 100% of the price paid by the investor for the mortgage servicing rights for any loans in the previously sold pools that paid off in full. The agreement terminates on July 31, 2018, or upon the Company giving 90 days notice to seller. In the third quarter of 2016, the loss on mortgage servicing rights of \$7.5 million includes a \$2.8 million charge for third quarter 2016 refinance activity and the remaining balance is primarily related to a reserve for potential future estimated premium recapture charges.

The following is a summary of certain components of servicing income, net as reported in the Company's consolidated statements of operations for the three and nine months ended September 30, 2016:

	For the Three Months Ended September 30, 2016		For the Nine Months Ended September 30, 2015	
Contractual servicing fees	\$ 4,755	\$ 3,014	\$ 10,981	\$ 5,702
Late and ancillary fees	41	33	115	91

Note 5.—Goodwill and Intangible Assets

Goodwill arises from the acquisition method of accounting for business combinations and represents the excess of the purchase price over the fair value of the net assets and other identifiable intangible assets acquired. Other intangible

assets with definite lives include trademarks, customer relationships, and non-compete agreements. In the first quarter of 2015, the Company acquired CCM and recorded \$104.6 million of goodwill and intangible assets of \$33.1 million, consisting of \$17.2 million for trademark, \$10.2 million for customer relationships and \$5.7 million for a non-compete agreement with the former owner of CCM. The purchase price allocation was prepared with the assistance of a third party valuation firm.

Goodwill, trademarks and other intangible assets are assessed annually for impairment or more frequently if events and circumstances indicate that the asset might be impaired. The carrying value of these intangible assets could be impaired if a significant adverse change in the use, life, or brand strategy of the asset is determined, or if a significant adverse change in the legal and regulatory environment, business or competitive climate occurs that would adversely impact the asset.

Table of Contents

Goodwill and other intangible assets deemed to have indefinite lives generated from purchase business combinations are not subject to amortization but are instead assessed for impairment on an ongoing basis. Impairment exists when the carrying value of goodwill exceeds its implied fair value. An impairment loss, if any, is measured as the excess of carrying value of the goodwill over the implied fair value of the goodwill and would be recorded in other expense in the consolidated statements of operations. Intangible assets with definite lives are amortized over their estimated lives using an amortization method that reflects the pattern in which the economic benefits of the asset are consumed.

For goodwill, the determination of fair value of a reporting unit involves, among other things, application of the income approach, which includes developing forecasts of future cash flows and determining an appropriate discount rate. Goodwill is considered a Level 3 nonrecurring fair value measurement.

The methodology used to determine the fair value of trademarks includes assumptions with inherent uncertainty, including projected sales volumes and related projected revenues, long-term growth rates, royalty rates that a market participant might assume and judgments regarding the factors to develop an applied discount rate. The carrying value of intangible assets is at risk of impairment if future projected revenues or long-term growth rates are lower than those currently projected, or if factors used in the development of a discount rate result in the application of a higher discount rate. The intangible assets are considered Level 3 nonrecurring fair value measurements.

As part of the acquisition of CCM, the purchase price of the intangible assets the Company acquired are listed below:

	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount at September 30, 2016	Remaining Life
Intangible assets:				
Trademark	\$ 17,251	\$ (1,754)	\$ 15,497	13.3
Customer relationships	10,170	(2,260)	7,910	5.3
Non-compete agreement	5,701	(2,281)	3,420	2.3
Total intangible assets acquired	\$ 33,122	\$ (6,295)	\$ 26,827	9.5

As part of the acquisition of CCM, the purchase price of other assets the Company acquired are listed below:

	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount at September 30, 2016	Remaining Life
Other assets:				
Developed software	\$ 2,719	\$ (859)	\$ 1,860	3.3

Table of Contents

Note 6.—Warehouse Borrowings

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

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

	Maximum Borrowing Capacity	Balance Outstanding At	
		September 30, 2016	December 31, 2015
Short-term borrowings:			
Repurchase agreement 1	\$ 150,000	\$ 149,498	\$ 63,368
Repurchase agreement 2	50,000	49,806	46,673
Repurchase agreement 3 (1)	225,000	157,838	122,242
Repurchase agreement 4	200,000	192,072	83,162
Repurchase agreement 5 (2)	175,000	174,343	10,171
Repurchase agreement 6 (3)	200,000	156,554	—
Total warehouse borrowings	\$ 1,000,000	\$ 880,111	\$ 325,616

-
- (1) As of September 30, 2016 and December 31, 2015, \$78.7 million and \$36.4 million, respectively, are attributable to financing facility advances made to the Company's warehouse customers. In October 2016, the maturity was extended to December 23, 2016.
- (2) In August 2016, the lender granted the Company an increase in the maximum borrowing capacity to \$175.0 million with a temporary increase to \$200.0 million until September 15, 2016. In April 2016, the maturity date was extended to March 1, 2017.
- (3) In September 2016, the lender granted the Company an increase in the maximum borrowing capacity to \$200.0 million until maturity date of June 30, 2017.

Note 7.—Term Financing

In June 2015, the Company and its subsidiaries, (IRES, IMC and Impac Warehouse Lending, Inc. (IWLI), collectively the (Borrowers)) entered into a Loan Agreement (Loan Agreement) with a lender (Lender) pursuant to which the Lender provided to the Borrowers a term loan in the aggregate principal amount of \$30.0 million (Term Financing) due and payable on December 19, 2016, which may be extended to December 18, 2017 at the Lender's discretion. In connection with the Term Financing, the Borrowers issued to the Lender a Term Note dated June 19, 2015. The Lender may in its discretion make additional advances not to exceed an aggregate amount outstanding of \$50.0 million. In June 2016, the maturity of the Term Financing was extended to June 16, 2017 and the Company paid an additional \$100 thousand extension fee, which is amortized using the effective yield method over the life of the term financing.

The proceeds from the Term Financing were used to pay off the working capital line of credit with a national bank (approximately \$4.0 million) and amounts under an existing master repurchase agreement with the Lender (approximately \$3.2 million). The Borrowers also paid the Lender an origination fee of \$300 thousand which is amortized using the effective yield method over the life of the term financing.

Interest on the Term Financing is payable monthly and accrues at a rate of LIBOR plus 8.5% per annum. As of September 30, 2016, amounts under the Term Financing may be prepaid at any time without penalty or premium. The Borrowers are subject to mandatory prepayment on the Term Financing based on a borrowing base formula that includes amounts under outstanding warehouse facilities, market value of mortgage servicing rights and residual securities and certain mortgage loans.

Table of Contents

The balance under the Term Financing as of September 30, 2016 and December 31, 2015 was \$29.9 million and \$29.7 million, respectively, net of debt issuance costs of \$129 thousand and \$284 thousand, respectively.

The obligations of the Borrowers under the Loan Agreement are secured by assets and a pledge of all of the capital stock of the operating subsidiaries IRES, IMC and IWLI pursuant to a Security Agreement dated as of June 19, 2015 between the Borrowers and the Lender (Security Agreement). As part of the Loan Agreement the Company received an acknowledgement agreement from FNMA and FHLMC to pledge the mortgage servicing rights to the Lender.

The Term Financing is subject to customary affirmative and negative covenants of the Borrowers. Upon an event of default, all outstanding amounts under the Term Financing may become immediately due and payable. An event of default also occurs upon a change of control, which means acquisition of more than 25% of the common stock of the Company, more than 50% of the common stock of any other Borrower, or the ability to elect a majority of such Borrower's directors or an event that triggers a violation of a change of control provision in any of the Borrowers' warehouse facilities.

Note 8.—Convertible Notes

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

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

Noteholders may convert all or a portion of the outstanding principal amount of the 2015 Convertible Notes into shares of the Company's common stock (Conversion Shares) at a rate of \$21.50 per share, subject to adjustment for stock splits and dividends (the Conversion Price). The Company has the right to convert the entire outstanding principal of the 2015 Convertible Notes into Conversion Shares at the Conversion Price if the market price per share of the common stock, as measured by the average volume-weighted closing stock price per share of the common stock on the NYSE MKT (or any other U.S. national securities exchange then serving as the principal such exchange on which the shares of common stock are listed), reaches the level of \$30.10 for any twenty (20) trading days in any period of thirty (30) consecutive trading days after the Closing Date. Upon conversion of the 2015 Convertible Notes by the Company, the entire amount of accrued and unpaid interest (and all other amounts owing) under the 2015 Convertible Notes are immediately due and payable. Furthermore, if the conversion of the 2015 Convertible Notes by the Company occurs prior to the third anniversary of the Closing Date, then the entire amount of interest under the 2015 Convertible Notes through the third anniversary is immediately due and payable. To the extent the Company pays any cash dividends on its shares of common stock prior to conversion of the 2015 Convertible Notes, upon conversion of the 2015 Convertible Notes, the Noteholders will also receive such dividends on an as-converted basis of the 2015 Convertible Notes less the amount of interest paid by the Company prior to such dividend.

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

time within such three year period.

15

Table of Contents

Note 9.—Securitized Mortgage Trusts

Securitized Mortgage Trust Assets

Securitized mortgage trust assets, which are recorded at their estimated fair value (FMV), are comprised of the following at September 30, 2016 and December 31, 2015:

	September 30, 2016	December 31, 2015
Securitized mortgage collateral	\$ 4,155,457	\$ 4,574,919
REO	14,062	19,589
Investment securities available-for-sale	—	26
Total securitized mortgage trust assets	\$ 4,169,519	\$ 4,594,534

Securitized Mortgage Trust Liabilities

Securitized mortgage trust liabilities, which are recorded at their estimated FMV, are comprised of the following at September 30, 2016 and December 31, 2015:

	September 30, 2016	December 31, 2015
Securitized mortgage borrowings	\$ 4,151,365	\$ 4,578,657
Derivative liabilities	24	1,669
Total securitized mortgage trust liabilities	\$ 4,151,389	\$ 4,580,326

Changes in fair value of net trust assets, including trust REO losses are comprised of the following for the three and nine months ended September 30, 2016 and 2015:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2016	2015	2016	2015
Change in fair value of net trust assets, excluding REO	\$ 2,511	\$ (568)	\$ 8,580	\$ 1,821
Losses from REO	(1,440)	(2,436)	(5,971)	(4,899)
Change in fair value of net trust assets, including trust REO gains (losses)	\$ 1,071	\$ (3,004)	\$ 2,609	\$ (3,078)

Note 10.—Fair Value of Financial Instruments

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

estimated fair value.

16

Table of Contents

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

	September 30, 2016				December 31, 2015			
	Carrying Amount	Estimated Fair Value			Carrying Amount	Estimated Fair Value		
		Level 1	Level 2	Level 3		Level 1	Level 2	Level 3
Assets								
Cash and cash equivalents	\$ 58,902	\$ 58,902	\$ —	\$ —	\$ 32,409	\$ 32,409	\$ —	\$ —
Restricted cash	9,928	9,928	—	—	3,474	3,474	—	—
Mortgage loans held-for-sale	849,521	—	849,521	—	310,191	—	310,191	—
Finance receivables	78,653	—	78,653	—	36,368	—	36,368	—
Mortgage servicing rights	87,413	—	—	87,413	36,425	—	—	36,425
Derivative assets, lending, net	27,734	—	414	27,320	9,273	—	89	9,184
Investment securities available-for-sale	—	—	—	—	26	—	—	26
Securitized mortgage collateral	4,155,457	—	—	4,155,457	4,574,919	—	—	4,574,919
Liabilities								
Warehouse borrowings	\$ 880,111	\$ —	\$ 880,111	\$ —	\$ 325,616	\$ —	\$ 325,616	\$ —
Term financing	29,871	—	—	29,871	29,716	—	—	29,716
Convertible notes	24,962	—	—	24,962	44,819	—	—	44,819
Contingent consideration	59,896	—	—	59,896	48,079	—	—	48,079
Long-term debt	39,835	—	—	39,835	31,898	—	—	31,898
Securitized mortgage borrowings	4,151,365	—	—	4,151,365	4,578,657	—	—	4,578,657
Derivative liabilities, securitized trusts	24	—	—	24	1,669	—	—	1,669
Derivative liabilities, lending, net	4,089	—	4,089	—	404	—	404	—

The fair value amounts above have been estimated by management using available market information and appropriate valuation methodologies. Considerable judgment is required to interpret market data to develop the estimates of fair value in both inactive and orderly markets. Accordingly, the estimates presented are not necessarily

indicative of the amounts that could be realized in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

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

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

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

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

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

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

Table of Contents

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

Fair Value Hierarchy

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

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

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

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

As a result of the lack of observable market data resulting from inactive markets, the Company has classified its investment securities available-for-sale, mortgage servicing rights, securitized mortgage collateral and borrowings, derivative assets and liabilities (trust and IRLCs), and long-term debt as Level 3 fair value measurements. Level 3 assets and liabilities measured at fair value on a recurring basis were approximately 83% and 99% and 94% and 99%, respectively, of total assets and total liabilities measured at estimated fair value at September 30, 2016 and December 31, 2015.

Recurring Fair Value Measurements

The Company assesses the financial instruments on a quarterly basis to determine the appropriate classification within the fair value hierarchy, as defined by ASC Topic 810. Transfers between fair value classifications occur when there are changes in pricing observability levels. Transfers of financial instruments among the levels occur at the beginning of the reporting period. There were no material transfers between our Level 1 and Level 2 classified instruments during the three and nine months ended September 30, 2016.

Table of Contents

The following tables present the Company's assets and liabilities that are measured at estimated fair value on a recurring basis, including financial instruments for which the Company has elected the fair value option at September 30, 2016 and December 31, 2015, based on the fair value hierarchy:

	Recurring Fair Value Measurements					
	September 30, 2016			December 31, 2015		
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Assets						
Investment securities available-for-sale	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 26
Mortgage loans held-for-sale	—	849,521	—	—	310,191	—
Derivative assets, lending, net (1)	—	414	27,320	—	89	9,184
Mortgage servicing rights	—	—	87,413	—	—	36,425
Securitized mortgage collateral	—	—	4,155,457	—	—	4,574,919
Total assets at fair value	\$ —	\$ 849,935	\$ 4,270,190	\$ —	\$ 310,280	\$ 4,620,554
Liabilities						
Securitized mortgage borrowings	\$ —	\$ —	\$ 4,151,365	\$ —	\$ —	\$ 4,578,657
Derivative liabilities, securitized trusts (2)	—	—	24	—	—	1,669
Long-term debt	—	—	39,835	—	—	31,898
Contingent consideration	—	—	59,896	—	—	48,079
Derivative liabilities, lending, net (3)	—	4,089	—	—	404	—
Total liabilities at fair value	\$ —	\$ 4,089	\$ 4,251,120	\$ —	\$ 404	\$ 4,660,303

(1) At September 30, 2016, derivative assets, lending, net included \$27.3 million in IRLCs and \$414 thousand in Hedging Instruments, respectively, and is included in other assets in the accompanying consolidated balance sheets. At December 31, 2015, derivative assets, lending, net included \$9.2 million in IRLCs and \$89 thousand in Hedging Instruments associated with the Company's mortgage lending operations, and is included in other assets in the accompanying consolidated balance sheet.

(2) At September 30, 2016 and December 31, 2015, derivative liabilities, securitized trusts, are included within trust liabilities in the accompanying consolidated balance sheets.

(3) At September 30, 2016 and December 31, 2015, derivative liabilities, lending, net are included in other liabilities in the accompanying consolidated balance sheets.

Table of Contents

The following tables present reconciliations for all assets and liabilities measured at estimated fair value on a recurring basis using significant unobservable inputs (Level 3) for the three months ended September 30, 2016 and 2015:

Level 3 Recurring Fair Value Measurements
For the Three Months Ended September 30, 2016

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

(1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities. Net interest income, including cash received and paid, was \$2.6 million for the three months ended September 30, 2016. The difference between accretion of interest income and expense and the amounts of interest income and expense recognized in the consolidated statements of operations is primarily from contractual interest on the securitized mortgage collateral and borrowings.

(2) Represents the amount of unrealized gains (losses) relating to assets and liabilities classified as Level 3 that are still held and reflected in the fair values at September 30, 2016.

Table of Contents

Level 3 Recurring Fair Value Measurements For the Three Months Ended September 30, 2015									
	Investment securities available for-sale	Securitized mortgage collateral	Securitized mortgage borrowings	Derivative liabilities, net, securitized trusts	Mortgage servicing rights	Interest rate lock commitment net	Long- term debt	Contingent consideration	Warrant
Fair value, June 30, 2015	\$ 81	\$ 4,979,433	\$ (4,977,150)	\$ (3,509)	\$ 44,244	\$ 8,406	\$ (31,438)	\$ (91,407)	\$ 165
Total gains (losses) included in earnings:									
Interest income (1)	2	18,930	—	—	—	—	—	—	—
Interest expense (1)	—	—	(53,552)	—	—	—	(225)	—	—
Change in fair value	(7)	(13,485)	13,051	(127)	(4,347)	4,613	—	14,473	(165)
Total (losses) gains included in earnings	(5)	5,445	(40,501)	(127)	(4,347)	4,613	(225)	14,473	(165)
Transfers in and/or out of Level 3	—	—	—	—	—	—	—	—	—
Purchases, issuances and settlements:									
Purchases	—	—	—	—	—	—	—	—	—
Issuances	—	—	—	—	23,384	—	—	—	—
Settlements	(26)	(188,473)	221,251	1,012	—	—	—	8,142	—
Fair value, September 30, 2015	\$ 50	\$ 4,796,405	\$ (4,796,400)	\$ (2,624)	\$ 63,281	\$ 13,019	\$ (31,663)	\$ (68,792)	\$ —
Unrealized gains (losses) still held (2)	\$ 50	\$ (1,143,833)	\$ 3,287,018	\$ (2,390)	\$ 63,281	\$ 13,019	\$ 39,100	\$ (68,792)	\$ —

- (1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities. Net interest income, including cash received and paid, was \$2.0 million for the three months ended September 30, 2015. The difference between accretion of interest income and expense and the amounts of interest income and expense recognized in the consolidated statements of operations is primarily from contractual interest on the securitized mortgage collateral and borrowings.
- (2) Represents the amount of unrealized gains (losses) relating to assets and liabilities classified as Level 3 that are still held and reflected in the fair values at September 30, 2015.

Table of Contents

The following tables present reconciliations for all assets and liabilities measured at estimated fair value on a recurring basis using significant unobservable inputs (Level 3) for the nine months ended September 30, 2016 and 2015:

Level 3 Recurring Fair Value Measurements
For the Nine Months Ended September 30, 2016

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

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

Table of Contents

Level 3 Recurring Fair Value Measurements
For the Nine Months Ended September 30, 2015

	Investment securities available for-sale	Securitized mortgage collateral	Securitized mortgage borrowings	Derivative liabilities, net, securitized trusts	Mortgage servicing rights	Interest rate lock commitment net	Long- term debt	Contingent consideration	Warrant
Fair value, December 31, 2014	\$ 92	\$ 5,249,639	\$ (5,245,860)	\$ (5,447)	\$ 24,418	\$ 2,884	\$ (22,122)	\$ —	\$ 84
Total gains (losses) included in earnings:									
Interest income (1)	9	49,719	—	—	—	—	—	—	—
Interest expense (1)	—	—	(160,249)	—	—	—	(880)	—	—
Change in fair value	33	6,918	(4,647)	(483)	(7,984)	10,135	(8,661)	22,752	(84)
Total (losses) gains included in earnings	42	56,637	(164,896)	(483)	(7,984)	10,135	(9,541)	22,752	(84)
Transfers in and/or out of Level 3	—	—	—	—	—	—	—	—	—
Purchases, issuances and settlements:									
Purchases	—	—	—	—	—	—	—	—	—
Issuances	—	—	—	—	76,119	—	—	(124,592)	—
Settlements	(84)	(509,871)	614,356	3,306	(29,272)	—	—	33,048	—
Fair value, September 30, 2015	\$ 50	\$ 4,796,405	\$ (4,796,400)	\$ (2,624)	\$ 63,281	\$ 13,019	\$ (31,663)	\$ (68,792)	\$ —

(1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities. Net interest income, including cash received and paid, was \$6.3 million for the nine months ended September 30, 2015. The difference between accretion of interest income and expense and the amounts of interest income and expense recognized in the consolidated statements of operations is primarily from contractual interest on the securitized mortgage collateral and borrowings.

The following table presents quantitative information about the valuation techniques and unobservable inputs applied to Level 3 fair value measurements for financial instruments measured at fair value on a recurring and non-recurring basis at September 30, 2016:

Financial Instrument Assets and liabilities backed by real estate Securitized mortgage collateral, and Securitized mortgage borrowings	Estimated Fair Value	Valuation Technique	Unobservable Input	Range of Inputs	Weighted Average
	\$ 4,155,457		Prepayment rates	2.5 - 23.1 %	6.7 %
	(4,151,365)		Default rates	0.2 - 10.4 %	2.4 %
			Loss severities	0.8 - 82.2 %	42.6 %

Edgar Filing: IMPAC MORTGAGE HOLDINGS INC - Form 10-Q

Other assets and liabilities						
Mortgage servicing rights	\$ 87,413	DCF	Discount rate	9.0 - 14.0 %	9.5	%
			Prepayment rates	5.1 - 84.6 %	12.5	%
Derivative liabilities, net, securitized trusts	(24)	DCF	1M forward LIBOR	0.5 - 1.9 %	N/A	
Derivative assets - IRLCs, net	27,320	Market pricing		13.6 -		
Long-term debt	(39,835)	DCF	Pull-through rate	99.9 %	85.5	%
Contingent consideration	(59,896)	DCF	Discount rate	11.0 %	11.0	%
			Discount rate	16.6 %	16.6	%
			Margins	1.3 - 2.5 %	2.1	%
			Probability of outcomes (1)	25.0 - 50.0 %	33.4	%

DCF = Discounted Cash Flow

1M = 1 Month

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

Table of Contents

For assets and liabilities backed by real estate, a significant increase in discount rates, default rates or loss severities would result in a significantly lower estimated fair value. The effect of changes in prepayment speeds would have differing effects depending on the seniority or other characteristics of the instrument. For other assets and liabilities, a significant increase in discount rates would result in a significantly lower estimated fair value. A significant increase in one-month LIBOR would result in a significantly higher estimated fair value for derivative liabilities, net, securitized trusts. The Company believes that the imprecision of an estimate could be significant.

The following tables present the changes in recurring fair value measurements included in net earnings (loss) for the three and nine months ended September 30, 2016 and 2015:

	Recurring Fair Value Measurements Changes in Fair Value Included in Net Earnings For the Three Months Ended September 30, 2016						
	Change in Fair Value of						Total
	Interest Income (1)	Interest Expense (1)	Net Trust Assets	Long-term Debt	Other Revenue and Expense	Gain on sale of loans, net	
Investment securities available-for-sale	\$ —	\$ —	\$ (21)	\$ —	\$ —	\$ —	\$ (21)
Securitized mortgage collateral	13,336	—	35,225	—	—	—	48,561
Securitized mortgage borrowings	—	(43,956)	(32,644)	—	—	—	(76,600)
Derivative liabilities, net, securitized trusts	—	—	(49)	(2)	—	—	(49)
Long-term debt	—	(204)	—	(8,641)	—	—	(8,845)
Mortgage servicing rights (3)	—	—	—	—	(8,224)	—	(8,224)
Contingent consideration	—	—	—	—	(24,806)	—	(24,806)
Mortgage loans held-for-sale	—	—	—	—	—	5,300	5,300
Derivative assets — IRLCs	—	—	—	—	—	8,017	8,017
Derivative liabilities — Hedging Instruments	—	—	—	—	—	(2,277)	(2,277)
Total	\$ 13,336	\$ (44,160)	\$ 2,511	\$ (8,641)	\$ (33,030)	\$ 11,040	\$ (58,944)

(1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities.

Edgar Filing: IMPAC MORTGAGE HOLDINGS INC - Form 10-Q

- (2) Included in this amount is \$280 thousand in changes in the fair value of derivative instruments, offset by \$329 thousand in cash payments from the securitization trusts for the three months ended September 30, 2016.
- (3) Included in loss on mortgage servicing rights in the consolidated statements of operations.

Recurring Fair Value Measurements
Changes in Fair Value Included in Net Earnings
For the Three Months Ended September 30, 2015

	Change in Fair Value of						Gain on sale of loans, net	Total
	Interest Income (1)	Interest Expense (1)	Net Trust Assets	long-term Debt	Other Revenue			
Investment securities available-for-sale	\$ 2	\$ —	\$ (7)	\$ —	\$ —	\$ —	\$ (5)	
Securitized mortgage collateral	18,930	—	(13,485)	—	—	—	5,445	
Securitized mortgage borrowings	—	(53,552)	13,051	—	—	—	(40,501)	
Derivative liabilities, net, securitized trusts	—	—	(127)	(2)	—	—	(127)	
Long-term debt	—	(225)	—	—	—	—	(225)	
Mortgage servicing rights (3)	—	—	—	—	(4,347)	—	(4,347)	
Warrant	—	—	—	—	(165)	—	(165)	
Contingent consideration	—	—	—	—	14,473	—	14,473	
Mortgage loans held-for-sale	—	—	—	—	—	6,678	6,678	
Derivative assets — IRLCs	—	—	—	—	—	4,613	4,613	
Derivative liabilities — Hedging Instruments	—	—	—	—	—	(3,658)	(3,658)	
Total	\$ 18,932	\$ (53,777)	\$ (568)	\$ —	\$ 9,961	\$ 7,633	\$ (17,819)	

- (1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities.
- (2) Included in this amount is \$835 thousand in change in the fair value of derivative instruments, offset by \$963 thousand in cash payments from the securitization trusts for the three months ended September 30, 2015.

Table of Contents

(3) Included in loss on mortgage servicing rights in the consolidated statements of operations.

	Recurring Fair Value Measurements						
	Changes in Fair Value Included in Net Earnings						
	For the Nine Months Ended September 30, 2016						
	Change in Fair Value of						Total
	Interest	Interest	Net Trust	Long-term	Other	Gain on sale	
	Income (1)	Expense (1)	Assets	Debt	Revenue and Expense	of loans, net	
Investment securities available-for-sale	\$ 2	\$ —	\$ 19	\$ —	\$ —	\$ —	\$ 21
Securitized mortgage collateral	46,540	—	27,780	—	—	—	74,320
Securitized mortgage borrowings	—	(141,927)	(19,020)	—	—	—	(160,947)
Derivative liabilities, net, securitized trusts	—	—	(199)	(2)	—	—	(199)
Long-term debt	—	(651)	—	(7,286)	—	—	(7,937)
Mortgage servicing rights (3)	—	—	—	—	(32,048)	—	(32,048)
Contingent consideration	—	—	—	—	(39,813)	—	(39,813)
Mortgage loans held-for-sale	—	—	—	—	—	19,572	19,572
Derivative assets — IRLCs	—	—	—	—	—	18,136	18,136
Derivative liabilities — Hedging Instruments	—	—	—	—	—	(3,518)	(3,518)
Total	\$ 46,542	\$ (142,578)	\$ 8,580	(4) \$ (7,286)	\$ (71,861)	\$ 34,190	\$ (132,413)

(1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities.

(2) Included in this amount is \$1.5 million in change in the fair value of derivative instruments, offset by \$1.7 million in cash payments from the securitization trusts for the nine months ended September 30, 2016.

(3) Included in loss on mortgage servicing rights in the consolidated statements of operations.

(4) For the nine months ended September 30, 2016, change in the fair value of net trust assets, excluding REO was \$8.6 million. Excluded from the \$10.3 million change in fair value of net trust assets, excluding REO, in the accompanying consolidated statement of cash flows is \$1.7 million in cash payments from the securitization trusts related to the Company's net derivative liabilities.

Edgar Filing: IMPAC MORTGAGE HOLDINGS INC - Form 10-Q

Recurring Fair Value Measurements
Changes in Fair Value Included in Net Earnings
For the Nine Months Ended September 30, 2015

	Interest Income (1)	Interest Expense (1)	Change in Fair Value of Net Trust Assets	long-term Debt	Other Revenue	Gain on sale of loans, net	Total
Investment securities available-for-sale	\$ 9	\$ —	\$ 33	\$ —	\$ —	\$ —	\$ 42
Securitized mortgage collateral	49,719	—	6,918	—	—	—	56,637
Securitized mortgage borrowings	—	(160,249)	(4,647)	—	—	—	(164,896)
Derivative liabilities, net, securitized trusts	—	—	(483) (2)	—	—	—	(483)
Long-term debt	—	(880)	—	(8,661)	—	—	(9,541)
Mortgage servicing rights (3)	—	—	—	—	(7,984)	—	(7,984)
Warrant	—	—	—	—	(84)	—	(84)
Contingent consideration	—	—	—	—	22,752	—	22,752
Mortgage loans held-for-sale	—	—	—	—	—	9,030	9,030
Derivative assets — IRLCs	—	—	—	—	—	10,135	10,135
Derivative liabilities — Hedging Instruments	—	—	—	—	—	(1,381)	(1,381)
Total	\$ 49,728	\$ (161,129)	\$ 1,821 (4)	\$ (8,661)	\$ 14,684	\$ 17,784	\$ (85,773)

(1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities.

(2) Included in this amount is \$2.7 million in change in the fair value of derivative instruments, offset by \$3.2 million in cash payments from the securitization trusts for the nine months ended September 30, 2015.

(3) Included in loss on mortgage servicing rights in the consolidated statements of operations.

Table of Contents

(4) For the nine months ended September 30, 2015, change in the fair value of net trust assets, excluding REO was \$1.8 million. Excluded from the \$5.0 million change in fair value of net trust assets, excluding REO, in the accompanying consolidated statement of cash flows is \$3.2 million in cash payments from the securitization trusts related to the Company's net derivative liabilities.

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

Investment securities available-for-sale—Investment securities available-for-sale are carried at fair value. The investment securities consist primarily of non-investment grade mortgage-backed securities. The fair value of the investment securities is measured based upon the Company's expectation of inputs that other market participants would use. Such assumptions include judgments about the underlying collateral, prepayment speeds, future credit losses, forward interest rates and certain other factors. Given the lack of observable market data as of September 30, 2016 and December 31, 2015 relating to these securities, the estimated fair value of the investment securities available-for-sale was measured using significant internal expectations of market participants' assumptions. Investment securities available-for-sale is considered a Level 3 measurement at September 30, 2016.

Mortgage servicing rights—The Company elected to carry its mortgage servicing rights arising from its mortgage loan origination operation at estimated fair value. The fair value of mortgage servicing rights is based upon market prices for similar instruments and a discounted cash flow model. The valuation model incorporates assumptions that market participants would use in estimating the fair value of servicing. These assumptions include estimates of prepayment speeds, discount rate, cost to service, escrow account earnings, contractual servicing fee income, prepayment and late fees, among other considerations. Mortgage servicing rights are considered a Level 3 measurement at September 30, 2016.

Mortgage loans held-for-sale—The Company elected to carry its mortgage loans held-for-sale originated or acquired at estimated fair value. Fair value is based on quoted market prices, where available, prices for other traded mortgage loans with similar characteristics, and purchase commitments and bid information received from market participants. Given the meaningful level of secondary market activity for mortgage loans, active pricing is available for similar assets and accordingly, the Company classifies its mortgage loans held-for-sale as a Level 2 measurement at September 30, 2016.

Securitized mortgage collateral—The Company elected to carry its securitized mortgage collateral at fair value. These assets consist primarily of non-conforming mortgage loans securitized between 2002 and 2007. Fair value measurements are based on the Company's internal models used to compute the net present value of future expected cash flows with observable market participant assumptions, where available. The Company's assumptions include its expectations of inputs that other market participants would use in pricing these assets. These assumptions include judgments about the underlying collateral, prepayment speeds, estimated future credit losses, forward interest rates, investor yield requirements and certain other factors. As of September 30, 2016, securitized mortgage collateral had UPB of \$5.1 billion, compared to an estimated fair value on the Company's balance sheet of \$4.2 billion. The aggregate UPB exceeds the fair value by \$0.9 billion at September 30, 2016. As of September 30, 2016, the UPB of loans 90 days or more past due was \$0.7 billion compared to an estimated fair value of \$0.3 billion. The aggregate UPB of loans 90 days or more past due exceed the fair value by \$0.4 billion at September 30, 2016. Securitized mortgage collateral is considered a Level 3 measurement at September 30, 2016.

Securitized mortgage borrowings—The Company elected to carry its securitized mortgage borrowings at fair value. These borrowings consist of individual tranches of bonds issued by securitization trusts and are primarily backed by non-conforming mortgage loans. Fair value measurements include the Company's judgments about the underlying collateral and assumptions such as prepayment speeds, estimated future credit losses, forward interest rates, investor yield requirements and certain other factors. As of September 30, 2016, securitized mortgage borrowings had an

outstanding principal balance of \$5.1 billion, net of \$2.2 billion in bond losses, compared to an estimated fair value of \$4.2 billion. The aggregate outstanding principal balance exceeds the fair value by \$0.9 billion at September 30, 2016. Securitized mortgage borrowings are considered a Level 3 measurement at September 30, 2016.

Table of Contents

Contingent consideration—Contingent consideration is applicable to the acquisition of CCM and is estimated and recorded at fair value at the acquisition date as part of purchase price consideration. Additionally, each reporting period, the Company estimates the change in fair value of the contingent consideration and any change in fair value is recognized in the Company's consolidated statements of operations if it is determined to not be a measurement period adjustment. The estimate of the fair value of contingent consideration requires significant judgment and assumptions to be made about future operating results, discount rates and probabilities of various projected operating result scenarios. During the three months ended September 30, 2016, the change in fair value of contingent consideration was related to an increase in projected volumes and earnings of CCM. Future revisions to these assumptions could materially change the estimated fair value of contingent consideration and materially affect the Company's financial results. Contingent consideration is considered a Level 3 measurement at September 30, 2016.

Long-term debt—The Company elected to carry all of its long-term debt (consisting of trust preferred securities and junior subordinated notes) at fair value. These securities are measured based upon an analysis prepared by management, which considered the Company's own credit risk, including settlements with trust preferred debt holders and discounted cash flow analysis. As of September 30, 2016, long-term debt had UPB of \$70.5 million compared to an estimated fair value of \$39.8 million. The aggregate UPB exceeds the fair value by \$31.7 million at September 30, 2016. The long-term debt is considered a Level 3 measurement at September 30, 2016.

Derivative assets and liabilities, Securitized trusts—For non-exchange traded contracts, fair value is based on the amounts that would be required to settle the positions with the related counterparties as of the valuation date. Valuations of derivative assets and liabilities are based on observable market inputs, if available. To the extent observable market inputs are not available, fair values measurements include the Company's judgments about future cash flows, forward interest rates and certain other factors, including counterparty risk. Additionally, these values also take into account the Company's own credit standing, to the extent applicable; thus, the valuation of the derivative instrument includes the estimated value of the net credit differential between the counterparties to the derivative contract. As of September 30, 2016, the notional balance of derivative assets and liabilities, securitized trusts was \$5.1 million. These derivatives are included in the consolidated securitization trusts, which are nonrecourse to the Company, and thus the economic risk from these derivatives is limited to the Company's residual interests in the securitization trusts. Derivative assets and liabilities, securitized trusts are considered a Level 3 measurement at September 30, 2016.

Derivative assets and liabilities, Lending—The Company's derivative assets and liabilities are carried at fair value as required by GAAP and are accounted for as free standing derivatives. The derivatives include IRLCs with prospective residential mortgage borrowers whereby the interest rate on the loan is determined prior to funding and the borrowers have locked in that interest rate. These commitments are determined to be derivative instruments in accordance with GAAP. The derivatives also include hedging instruments (typically TBA MBS) used to hedge the fair value changes associated with changes in interest rates relating to its mortgage lending originations as well as mortgage servicing rights. The Company hedges the period from the interest rate lock (assuming a fall-out factor) to the date of the loan sale. The estimated fair value of IRLCs are based on underlying loan types with similar characteristics using the TBA MBS market, which is actively quoted and easily validated through external sources. The data inputs used in this valuation include, but are not limited to, loan type, underlying loan amount, note rate, loan program, and expected sale date of the loan, adjusted for current market conditions. These valuations are adjusted at the loan level to consider the servicing release premium and loan pricing adjustments specific to each loan. For all IRLCs, the base value is then adjusted for the anticipated Pull-through Rate. The anticipated Pull-through Rate is an unobservable input based on historical experience, which results in classification of IRLCs as a Level 3 measurement at September 30, 2016.

The fair value of the Hedging Instruments is based on the actively quoted TBA MBS market using observable inputs related to characteristics of the underlying MBS stratified by product, coupon and settlement date. Therefore, the Hedging Instruments are classified as a Level 2 measurement at September 30, 2016.

Table of Contents

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

	Notional Amount		Total Gains (Losses) (1) For the Three Months Ended		Total Gains (Losses) (1) For the Nine Months Ended	
	September 30, 2016	September 30, 2015	September 30, 2016	September 30, 2015	September 30, 2016	September 30, 2015
Derivative – IRLC's	\$ 1,207,565	\$ 664,890	\$ 8,017	\$ 4,613	\$ 18,136	\$ 10,135
Derivative – TBA MBS	882,760	550,210	(5,279)	(10,405)	(22,529)	(9,834)

(1) Amounts included in gain on sale of loans, net within the accompanying consolidated statements of operations. Warrant— Upon entering an arrangement to facilitate the Company's ability to offer Non-QM mortgage products, a warrant to purchase up to 9.9% of Impac Mortgage Corp. was issued. The warrant expired in August 2015 and was not exercised. The estimated fair value of the warrant was based on a model incorporating various assumptions including expected future book value of Impac Mortgage Corp., the probability of the warrant being exercised, volatility, expected term and certain other factors.

Nonrecurring Fair Value Measurements

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

The following tables present financial and non-financial assets and liabilities measured using nonrecurring fair value measurements at September 30, 2016 and 2015, respectively:

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

(1) Total losses reflect losses from all nonrecurring measurements during the period.

(2) Balance represents REO at September 30, 2016 which has been impaired subsequent to foreclosure. For the three and nine months ended September 30, 2016, the \$1.4 million and \$6.0 million loss, respectively, represents additional impairment write-downs attributable to higher expected loss severities on properties held during the period which resulted in a decrease to the net realizable value (NRV).

(3) For the three and nine months ended September 30, 2016, the Company recorded \$200 thousand and \$815 thousand in income tax expense resulting from impairment write-downs of deferred charge based on changes in estimated cash flows and lives of the related mortgages retained in the securitized mortgage collateral.

	Non-recurring Fair Value Measurements			Total Gains (Losses) (1)	Total Gains (Losses) (1)
	September 30, 2015			For the Three Months Ended	For the Nine Months Ended
	Level 1	Level 2	Level 3	September 30, 2015	September 30, 2015
REO (2)	\$ —	\$ 2,066	\$ —	\$ (2,436)	\$ (4,900)
Lease liability (3)	—	—	(984)	(14)	(53)
Deferred charge (4)	—	—	10,467	(421)	(1,054)

(1) Total losses reflect losses from all nonrecurring measurements during the period.

Table of Contents

- (2) Balance represents REO at September 30, 2015 which has been impaired subsequent to foreclosure. For the three and nine months ended September 30, 2015, the \$2.4 million and \$4.9 million loss, respectively, represents additional impairment write-downs attributable to higher expected loss severities on properties held during the period which resulted in a decrease to the NRV.
- (3) For the three and nine months ended September 30, 2015, the Company recorded \$14 thousand and \$53 thousand expense, resulting from changes in lease liabilities as a result of changes in our expected minimum future lease payments.
- (4) For the three and nine months ended September 30, 2015, the Company recorded \$421 thousand and \$1.1 million in income tax expense resulting from impairment write-downs of deferred charge based on changes in estimated cash flows and lives of the related mortgages retained in the securitized mortgage collateral.

Real estate owned—REO consists of residential real estate acquired in satisfaction of loans. Upon foreclosure, REO is adjusted to the estimated fair value of the residential real estate less estimated selling and holding costs, offset by expected contractual mortgage insurance proceeds to be received, if any. Subsequently, REO is recorded at the lower of carrying value or estimated fair value less costs to sell. REO balance representing REOs which have been impaired subsequent to foreclosure are subject to nonrecurring fair value measurement and included in the nonrecurring fair value measurements tables. Fair values of REO are generally based on observable market inputs, and considered Level 2 measurements at September 30, 2016.

Lease liability— In January 2016, an amendment to the Company’s lease became effective modifying certain terms as well as extending the lease to 2024. The modification of the lease effectively eliminated the shortfall the Company had been recording as lease impairment attributable to the office space the Company was subletting associated with the previously discontinued operations. This liability was considered a Level 3 measurement at September 30, 2015.

Deferred charge— Deferred charge represents the deferral of income tax expense on inter-company profits that resulted from the sale of mortgages from taxable subsidiaries to IMH in prior years. The Company evaluates the deferred charge for impairment quarterly using internal estimates of estimated cash flows and lives of the related mortgages retained in the securitized mortgage collateral. If the deferred charge is determined to be impaired, it is recognized as a component of income tax expense. For the the three and nine months ended September 30, 2016, the Company recorded \$200 thousand and \$815 thousand, respectively, in income tax expense resulting from deferred charge impairment write-downs based on changes in estimated fair value of securitized mortgage collateral. Deferred charge is considered a Level 3 measurement at September 30, 2016.

Note 11.—Income Taxes

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

The Company recorded income tax benefit of \$130 thousand and an expense of \$728 thousand for the the three and nine months ended September 30, 2016 primarily the result of a return to provision adjustment for the 2015 tax return booked in the third quarter, amortization of the deferred charge, federal alternative minimum tax (AMT), and state income taxes from states where the Company does not have net operating loss carryforwards or state minimum taxes, including AMT. For the the three and nine months ended September 30, 2015, the Company recorded income tax expense (benefit) of \$781 thousand and (\$22.9) million, respectively. For the three months ended September 30, 2015,

the Company recorded amortization of the deferred charge and an increase in current income tax provision based upon an estimated increase in federal AMT and state income taxes. For the nine months ended September 30, 2015, the Company recorded a benefit of \$24.4 million primarily the result of a reversal of valuation allowance partially offset by

29

Table of Contents

AMT, amortization of the deferred charge and state income taxes from states where the Company does not have net operating loss carryforwards or state minimum taxes, including AMT. The deferred charge represents the deferral of income tax expense on inter-company profits that resulted from the sale of mortgages from taxable subsidiaries to IMH prior to 2008. The deferred charge is amortized and/or impaired, which does not result in any tax liability to be paid. The deferred charge is included in other assets in the accompanying consolidated balance sheets and is amortized as a component of income tax expense in the accompanying consolidated statements of operations.

Note 12.—Reconciliation of Earnings Per Share

Basic net earnings per share is computed by dividing net earnings available to common stockholders (numerator) by the weighted average number of vested, common shares outstanding during the period (denominator). Diluted net earnings per share is computed on the basis of the weighted average number of shares of common stock outstanding plus the effect of dilutive potential common shares outstanding during the period using the if-converted method. Dilutive potential common shares include shares issuable upon conversion of Convertible Notes, dilutive effect of outstanding stock options and deferred stock units (DSUs).

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2016	2015	2016	2015
Numerator for basic earnings per share:				
Net earnings	\$ 16,498	\$ 19,309	\$ 29,729	\$ 70,090
Numerator for diluted earnings per share:				
Net earnings	\$ 16,498	\$ 19,309	\$ 29,729	\$ 70,090
Interest expense attributable to convertible notes	457	844	1,997	1,875
Net earnings plus interest expense attributable to convertible notes	\$ 16,955	\$ 20,153	\$ 31,726	\$ 71,965
Denominator for basic earnings per share (1):				
Basic weighted average common shares outstanding during the period	12,920	10,242	12,241	10,019
Denominator for diluted earnings per share (1):				
Basic weighted average common shares outstanding during the period	12,920	10,242	12,241	10,019
Net effect of dilutive convertible notes	1,163	3,002	1,426	2,461
Net effect of dilutive stock options and DSU's	320	354	306	357
Diluted weighted average common shares	14,403	13,598	13,973	12,837
Net earnings per common share:				
Basic	\$ 1.28	\$ 1.89	\$ 2.43	\$ 7.00
Diluted	\$ 1.18	\$ 1.48	\$ 2.27	\$ 5.61

(1) Number of shares presented in thousands.

For the three and nine months ended September 30, 2016 there were 842 thousand anti-dilutive stock options outstanding. There were 367 thousand anti-dilutive stock options outstanding for the three and nine months ended September 30, 2015.

Table of Contents

Note 13.—Segment Reporting

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

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

Statement of Operations Items for the Three Months Ended September 30, 2015:	Mortgage Lending	Real Estate Services	Long-term Portfolio	Corporate and other	Consolidated
Gain on sale of loans, net	\$ 47,274	\$ —	\$ —	\$ —	\$ 47,274
Real estate services fees, net	—	2,775	—	—	2,775
Servicing income, net	2,432	—	—	—	2,432
Loss on mortgage servicing rights	(4,818)	—	—	—	(4,818)
Other revenue	(145)	—	79	55	(11)
Accretion of contingent consideration	(2,424)	—	—	—	(2,424)
Change in fair value of contingent consideration	16,897	—	—	—	16,897
Other expense	(35,827)	(1,447)	(263)	(1,613)	(39,150)
Other income (expense)	658	—	(1,936)	(1,607)	(2,885)
Net earnings (loss) before income taxes	\$ 24,047	\$ 1,328	\$ (2,120)	\$ (3,165)	\$ 20,090
Income tax expense					781
Net earnings					\$ 19,309

Edgar Filing: IMPAC MORTGAGE HOLDINGS INC - Form 10-Q

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

Table of Contents

Statement of Operations Items for the Nine Months Ended September 30, 2015:	Mortgage Lending	Real Estate Services	Long-term Portfolio	Corporate and other	Consolidated
Gain on sale of loans, net	\$ 133,018	\$ —	\$ —	\$ —	\$ 133,018
Real estate services fees, net	—	7,872	—	—	7,872
Servicing income, net	4,083	—	—	—	4,083
Loss on mortgage servicing rights	(14,176)	—	—	—	(14,176)
Other revenue	(25)	—	203	105	283
Accretion of contingent consideration	(5,471)	—	—	—	(5,471)
Change in fair value of contingent consideration	28,223	—	—	—	28,223
Other expense	(86,099)	(4,422)	(611)	(5,858)	(96,990)
Other income (expense)	1,673	—	(8,281)	(2,996)	(9,604)
Net earnings (loss) before income taxes	\$ 61,226	\$ 3,450	\$ (8,689)	\$ (8,749)	\$ 47,238
Income tax benefit					(22,852)
Net earnings					\$ 70,090

Balance Sheet Items as of:	Mortgage Lending	Real Estate Services	Long-term Mortgage Portfolio	Corporate and other	Consolidated
Total Assets at September 30, 2016 (1)	\$ 1,215,652	\$ 4,915	\$ 4,178,938	\$ 60,328	\$ 5,459,833
Total Assets at December 31, 2015(1)	\$ 573,648	\$ 3,933	\$ 4,604,701	\$ 28,570	\$ 5,210,852

(1) All segment asset balances exclude intercompany balances.

Note 14.—Commitments and Contingencies

Legal Proceedings

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

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

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

The Company is a party to other litigation and claims which are normal in the course of our operations. While the results of such other litigation and claims cannot be predicted with certainty, we believe the final outcome of such matters will not have a material adverse effect on our financial condition or results of operations. The Company believes that it has meritorious defenses to the claims and intends to defend these claims vigorously and as such the Company

Table of Contents

believes the final outcome of such matters will not have a material adverse effect on its financial condition or results of operations. Nevertheless, litigation is uncertain and the Company may not prevail in the lawsuits and can express no opinion as to their ultimate resolution. An adverse judgment in any of these matters could have a material adverse effect on the Company's financial position and results of operations.

Please refer to IMH's report on Form 10-K for the year ended December 31, 2015 for a description of litigation and claims.

Repurchase Reserve

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

The following table summarizes the repurchase reserve activity related to previously sold loans for the nine months ended September 30, 2016 and year ended December 31, 2015:

	September 30, 2016	December 31, 2015
Beginning balance	\$ 5,236	\$ 5,714
Provision for repurchases	778	1,012
Settlements	120	(1,490)
Total repurchase reserve	\$ 6,134	\$ 5,236

Short-Term Loan Commitments

The Company uses a portion of its warehouse borrowing capacity to provide secured short-term revolving financing to small and medium-size mortgage originators to finance mortgage loans from the closing of the mortgage loans until sold to investors (Finance Receivables). As of September 30, 2016, the warehouse lending operations had warehouse lines to non-affiliated customers totaling \$156.5 million, of which there was an outstanding balance of \$78.7 million in finance receivables compared to \$36.4 million as of December 31, 2015. The finance receivables are generally secured by residential mortgage loans as well as personal guarantees.

Note 15.—Equity and Share Based Payments

Equity

As further described in Note 8. – Convertible Notes, in January 2016, the Company elected to exercise its option to convert the Notes to common stock. The conversion resulted in the Company issuing an aggregate of 1,839,080 shares of common stock at a conversion price of \$10.875 per share.

The Company initiated an equity offering program (EOP) on December 3, 2015 by filing a prospectus supplement with the Securities and Exchange Commission (SEC) under its shelf registration. The EOP allows the Company to offer

and sell, from time to time, up to \$25.0 million of its common stock in negotiated transactions or transactions that are deemed to be "at the market offerings", as defined in Rule 415 under the Securities Act of 1933, as amended, including sales made directly on the NYSE MKT or sales made to or through a market maker other than on an exchange.

During the nine months ended September 30, 2016, the Company sold 361,429 shares of its common stock through the EOP at an average price of \$14.05 per share, for which it received proceeds of \$5.0 million, net of \$102 thousand in sales commission.

Table of Contents

On September 15, 2016, the Company entered into an underwriting agreement (Underwriting Agreement) with JMP Securities LLC (Underwriter) pursuant to which the Company sold 3,000,000 shares of common stock at a public offering price of \$13.00 per share. In addition, under the terms of the Underwriting Agreement, the Underwriter exercised its right to purchase an additional 450,000 shares of common stock. The shares were sold pursuant to a prospectus, dated May 28, 2015, and a prospectus supplement, dated September 15, 2016, in connection with a takedown from the Company's shelf registration statement on Form S-3 (File No. 333-204513) (Registration Statement), declared effective by the U.S. SEC on June 16, 2015.

The net proceeds to the Company from the offering were approximately \$42.6 million after deducting underwriting discounts and commissions and estimated aggregate offering expenses of \$200 thousand. The Company intends to use the net proceeds from the offering for general corporate purpose, including working capital and development costs, such as retention of servicing on new originations and to grow market share and geographic scope within the CashCall Mortgage retail channel, as well as continued growth in the correspondent and wholesale lending channels.

Share Based Payments

There were 342,000 stock options granted during the three and nine months ended September 30, 2016.

The following table summarizes activity, pricing and other information for the Company's stock options for the nine months ended September 30, 2016:

	Number of Shares	Weighted- Average Exercise Price
Options outstanding at beginning of period	1,115,280	\$ 11.85
Options granted	342,000	17.40
Options exercised	(38,620)	5.45
Options forfeited/cancelled	(20,583)	15.67
Options outstanding at end of period	1,398,077	13.33
Options exercisable at end of period	710,239	\$ 10.20

As of September 30, 2016, there was approximately \$4.1 million of total unrecognized compensation cost related to stock option compensation arrangements granted under the plan, net of estimated forfeitures. That cost is expected to be recognized over the remaining weighted average period of 2.2 years.

There were 342,000 and 405,800 options granted during the nine months ended September 30, 2016 and 2015, respectively. For the nine months ended September 30, 2016 and 2015, the aggregate grant-date fair value of stock options granted was \$2.7 million and approximately \$3.8 million, respectively.

The following table summarizes activity, pricing and other information for the Company's DSU's, also referred to as deferred stock units as the issuance of the stock is deferred until termination of service, for the nine months ended September 30, 2016:

	Number of Shares	Weighted- Average Grant Date Fair Value
DSU's outstanding at beginning of period	80,750	\$ 9.36
DSU's granted	5,000	17.40
DSU's exercised	—	—
DSU's forfeited/cancelled	—	—
DSU's outstanding at end of period	85,750	\$ 9.83

Table of Contents

As of September 30, 2016, there was approximately \$81 thousand of total unrecognized compensation cost related to the DSU compensation arrangements granted under the plan. That cost is expected to be recognized over a weighted average period of 2.8 years.

Note 16.—Subsequent Events

In October 2016, the Company, through IRES and its subsidiaries, entered into a Mortgage Loan Participation Sale Agreement with a lender providing a \$100 million facility. This facility provides liquidity for recently sold mortgage-backed securities up to the mortgage-backed securities settlement date. The interest rate relating to this agreement is LIBOR plus 1.5% subject to a floor of 1.5% and expires in October 2017. Under the terms of this facility, IRES and its subsidiaries are required to maintain various financial and other covenants.

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

Table of Contents

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

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

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

Forward-Looking Statements

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

For a discussion of these and other risks and uncertainties that could cause actual results to differ from those contained in the forward-looking statements, see "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Company's Annual Report on Form 10-K for the period ended December 31, 2015, and other reports we file under the Securities Exchange Act of 1934. This document speaks only as of its date and we do not undertake, and specifically disclaim any obligation, to release publicly the results of any revisions that may be made to any forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date of such statements.

The Mortgage Industry and Discussion of Relevant Fiscal Periods

The mortgage industry is subject to current events that occur in the financial services industry including changes to regulations and compliance requirements that result in uncertainty surrounding the actions of states, municipalities and

new government agencies, including the Consumer Financial Protection Bureau (CFPB) and Federal Housing Finance Agency (FHFA). These events can also include changes in economic indicators, interest rates, price competition, geographic shifts, disposable income, housing prices, market liquidity, market anticipation, and customer perception, as well as others. The factors that affect the industry change rapidly and can be unforeseeable making it difficult to predict and manage an operation in the financial services industry.

Table of Contents

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

Selected Financial Results

	For the Three Months Ended			For the Nine Months Ended	
	September 30, 2016	June 30, 2016	September 30, 2015	September 30, 2016	September 30, 2015
Revenues:					
Gain on sale of loans, net	\$ 113,158	\$ 78,822	\$ 47,274	\$ 245,849	\$ 133,018
Real estate services fees, net	2,678	1,995	2,775	6,773	7,872
Servicing income, net	3,789	2,803	2,432	8,680	4,083
Loss on mortgage servicing rights	(15,857)	(14,482)	(4,818)	(41,249)	(14,176)
Other	225	75	(11)	453	283
Total revenues	103,993	69,213	47,652	220,506	131,080
Expenses:					
Personnel expense	38,467	30,592	21,315	93,025	56,883
Business promotion	10,350	11,286	10,735	30,828	19,628
General, administrative and other	7,736	8,842	7,100	23,742	20,479
Accretion of contingent consideration	1,591	1,759	2,424	5,244	5,471
Change in fair value of contingent consideration	23,215	8,412	(16,897)	34,569	(28,223)
Total expenses	81,359	60,891	24,677	187,408	74,238
Operating income:	22,634	8,322	22,975	33,098	56,842
Other income (expense):					
Net interest income	1,304	833	119	2,036	2,135
Change in fair value of long-term debt	(8,641)	1,354	—	(7,286)	(8,661)
Change in fair value of net trust assets	1,071	2,165	(3,004)	2,609	(3,078)
Total other (expense) income	(6,266)	4,352	(2,885)	(2,641)	(9,604)
Net earnings before income taxes	16,368	12,674	20,090	30,457	47,238
Income tax (benefit) expense	(130)	423	781	728	(22,852)
Net earnings	\$ 16,498	\$ 12,251	\$ 19,309	\$ 29,729	\$ 70,090
Diluted weighted average common shares					
	14,403	13,863	13,598	13,973	12,837
Diluted earnings per share	\$ 1.18	\$ 0.92	\$ 1.48	\$ 2.27	\$ 5.61

Status of Operations

Summary Highlights

Edgar Filing: IMPAC MORTGAGE HOLDINGS INC - Form 10-Q

- We successfully raised capital issuing 3.4 million shares of common stock at a public offering price of \$13.00 per share generating net proceeds of \$42.6 million.
- Mortgage lending volumes increased in the third quarter of 2016 to \$4.2 billion from \$3.2 billion in the second quarter of 2016 and \$2.3 billion in the third quarter of 2015.
- Mortgage servicing portfolio increased to \$9.5 billion at September 30, 2016 from \$6.6 billion at June 30, 2016 and \$3.6 billion at December 31, 2015.
- Mortgage servicing rights increased to \$87.4 million at September 30, 2016 from \$54.7 million at June 30, 2016 and \$36.4 million at December 31, 2015.

Table of Contents

For the third quarter of 2016, the Company reported net earnings of \$16.5 million or \$1.18 per diluted common share, as compared to net earnings of \$19.3 million or \$1.48 per diluted common share for the third quarter of 2015, and \$12.3 million or \$0.92 per diluted common share for the second quarter of 2016. For the third quarter of 2016, operating income, excluding the changes in contingent consideration, as shown below, increased to \$47.4 million as compared to \$8.5 million in the third quarter of 2015, and \$18.5 million in the second quarter of 2016.

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

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

	For the Three Months Ended			For the Nine Months Ended	
	September 30, 2016	June 30, 2016	September 30, 2015	September 30, 2016	September 30, 2015
Net earnings:	\$ 16,498	\$ 12,251	\$ 19,309	\$ 29,729	\$ 70,090
Total other (expense) income	6,266	(4,352)	2,885	2,641	9,604
Income tax (benefit) expense	(130)	423	781	728	(22,852)
Operating income:	\$ 22,634	\$ 8,322	\$ 22,975	\$ 33,098	\$ 56,842
Accretion of contingent consideration	1,591	1,759	2,424	5,244	5,471
Change in fair value of contingent consideration	23,215	8,412	(16,897)	34,569	(28,223)
Operating income excluding changes in contingent consideration	\$ 47,440	\$ 18,493	\$ 8,502	\$ 72,911	\$ 34,090
Diluted weighted average common shares	14,403	13,863	13,598	13,973	12,837
Diluted operating income excluding changes in contingent consideration per share	\$ 3.29	\$ 1.33	\$ 0.63	\$ 5.22	\$ 2.66
Diluted earnings per share	\$ 1.18	\$ 0.92	\$ 1.48	\$ 2.27	\$ 5.61
Adjustments:					
Total other (expense) income (1)	0.40	(0.36)	0.15	0.05	0.60
Income tax (benefit) expense	(0.01)	0.03	0.06	0.05	(1.78)
Accretion of contingent consideration	0.11	0.13	0.18	0.38	0.43
Change in fair value of contingent consideration	1.61	0.61	(1.24)	2.47	(2.20)

Diluted operating income excluding changes in contingent consideration per share	\$ 3.29	\$ 1.33	\$ 0.63	\$ 5.22	\$ 2.66
--	---------	---------	---------	---------	---------

Operating income, excluding the changes in contingent consideration, increased to \$47.4 million or \$3.29 per diluted common share for the third quarter of 2016 as compared to \$8.5 million or \$0.63 per diluted common share in the third quarter of 2015, and \$18.5 million or \$1.33 per diluted common share in the second quarter of 2016. The \$28.9 million increase in operating income in the third quarter of 2016, as compared to the second quarter of 2016, was

Table of Contents

primarily due to a \$34.3 million increase in gain on sale of loans from a 30% increase in volume (as discussed below) combined with a 25 basis point “bps” increase in gain on sale margins to 268 bps in the quarter. This increase in gain on sale of loans was offset primarily by an increase in loss on mortgage servicing rights (MSR) of \$15.9 million, in the third quarter, as discussed below.

The contingent consideration liability represents the estimated fair value of the expected future earn-out payments to be paid to the seller of the CCM operations which were acquired in the first quarter of 2015. In the third quarter of 2016, we updated assumptions based on current market conditions resulting in an increase in projected volumes of CCM and in turn a higher estimated value of the contingent consideration to the seller of CCM. As a result, we recorded a change in the fair value of the contingent consideration in the third quarter increasing the contingent consideration liability by \$23.2 million over the remaining earn-out period of five quarters. Even though this projected increase in mortgage volume for CCM is a favorable development, as required by GAAP, it resulted in a corresponding charge to earnings of \$23.2 million in the third quarter of 2016.

Originations

(in millions)	For the Three Months Ended			September 30, 2015	September 30, 2015	
	September 30, 2016	June 30, 2016	% Change		%	% Change
Originations	\$ 4,217.0	\$ 3,247.4	30 %	\$ 2,303.2	83 %	%

Mortgage lending volumes increased in the third quarter of 2016 to \$4.2 billion from \$3.2 billion in the second quarter of 2016 and from \$2.3 billion in the third quarter of 2015. Of the \$4.2 billion in total originations, approximately \$3.3 billion, or 78%, was originated through the CCM retail channel.

(in millions)	For the Three Months Ended			September 30, 2015	September 30, 2015	
	September 30, 2016	June 30, 2016	% Change		%	% Change
Retail	\$ 3,273.7	\$ 2,493.0	31 %	\$ 1,285.7	155 %	%
Correspondent	583.2	419.9	39 %	608.5	(4) %	%
Wholesale	360.1	334.5	8 %	409.0	(12) %	%
Total originations	\$ 4,217.0	\$ 3,247.4	30 %	\$ 2,303.2	83 %	%

As a result of the attractive low mortgage interest rates, CCM has continued to be successful focusing on refinance volume. To the extent interest rates stay low, CCM originations will continue to be predominantly refinance concentrated. In the future, if interest rates rise, there may be an eventual decline in refinance volumes. However, we believe that our efforts to expand the national lending footprint, combined with greater emphasis on products offered through our other channels including government insured and NonQM products, may unlock opportunities to greatly diversify CCM’s retail loan production and increase our mortgage lending division’s total production.

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

Originations by Loan Type:

Edgar Filing: IMPAC MORTGAGE HOLDINGS INC - Form 10-Q

(in millions)	For the Three Months Ended September 30,			For the Nine Months Ended September 30,		
	2016	2015	% Change	2016	2015	% Change
Conventional	\$ 3,707.1	\$ 1,713.4	116 %	\$ 8,322.9	\$ 5,772.9	44 %
Government (1)	439.2	527.5	(17) %	1,281.7	1,421.7	(10) %
Other (2)	70.7	62.3	13 %	209.0	125.7	66 %
Total originations	4,217.0	2,303.2	83 %	9,813.6	7,320.3	34 %

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

39

Table of Contents

(2) Includes \$68.9 million and \$203.3 million of NonQM mortgages originated during the the three and nine months ended September 30, 2016, respectively.

We believe there is an underserved mortgage market for borrowers with good credit who may not meet the qualified mortgage (QM) guidelines set out by the Dodd-Frank Wall Street Reform and Consumer Protection Act. During 2014, we rolled out and began originating NonQM loans which increased in volume to \$132.4 million during 2015. During the first nine months of 2016, NonQM originations were \$203.3 million. Applications for NonQM loans has slowed during the quarter as a result of the current low mortgage interest rate environment. A decline in mortgage interest rates generally increases the volume of conventional refinance products over NonQM loans.

We have recently simplified the origination process for prospective NonQM borrowers. We believe these changes will better meet the needs of credit worthy borrowers unable to obtain mortgage financing through traditional agency or government mortgage programs. We have established strict lending guidelines, including determining the prospective borrowers' ability to repay the mortgage, which we believe will keep delinquencies and foreclosures at acceptable levels. We continue to refine our guidelines to expand our reach to the underserved market of credit worthy borrowers who can fully document and substantiate an ability to repay mortgage loans, but unable to obtain financing through traditional programs (QM loans), for example self-employed borrowers. Additionally, we relaunched our NonQM loan programs as "The Intelligent NonQM Mortgage, Engineered with Common Sense", to better communicate our NonQM loan value proposition to consumers, brokers, sellers and investors.

In 2014, we established a relationship with an institution that provided us with the initial exit strategy for NonQM loans. Under this arrangement, to date this investor has acquired \$229.2 million in NonQM loans. As of the third quarter of 2016, the investor is no longer purchasing NonQM loans, but we continue to have a relationship with them by which they are providing the Company with debt financing. This institution has continued to purchase a small amount of NonQM loans on a flow basis through September 2016, but we expect the sales of NonQM loans to this institution to end in the near future. However, in recent months, we have established new relationships with other investors interested in purchasing NonQM loan products including recent sales in second and third quarters of 2016. We will continue to seek out new investor relationships for these products which we believe will give us more flexibility in originating these loans.

(in millions)	For the Three Months Ended				For the Nine Months Ended			
	September 30,				September 30,			
	2016	%	2015	%	2016	%	2015	%
Refinance	\$ 3,756.8	89 %	\$ 1,732.9	75 %	\$ 8,554.0	87 %	\$ 6,000.9	82 %
Purchase	460.2	11 %	570.3	25 %	1,259.6	13 %	1,319.4	18 %
Total originations	\$ 4,217.0	100 %	\$ 2,303.2	100 %	\$ 9,813.6	100 %	\$ 7,320.3	100 %

During the third quarter of 2016, refinance volume increased approximately \$937.4 million or 33% as compared to the second quarter of 2016 and increased \$2.0 billion or 117% compared to the third quarter of 2015. This was primarily the result of the recent decline in mortgage interest rates which began during the first quarter of 2016.

To mitigate against reduced refinance volumes with the eventual expected increase in mortgage rates, we are focusing on opportunities that are intended to create diversity in our revenue streams. Our efforts to expand our NonQM volumes as well as increase our geographic footprint of our originations are part of this strategy.

Mortgage servicing portfolio

Edgar Filing: IMPAC MORTGAGE HOLDINGS INC - Form 10-Q

(in millions)	September 30, 2016	June 30, 2016	% Change		December 31, 2015	% Change		September 30, 2015	% Change	
Mortgage servicing portfolio	\$ 9,450.7	\$ 6,641.5	42	%	\$ 3,570.7	165	%	\$ 6,088.0	55	%

The mortgage servicing portfolio increased to \$9.5 billion at September 30, 2016 as compared to \$6.6 billion at June 30, 2016 and \$3.6 billion at December 31, 2015. The increase was due to servicing retained loan sales of \$9.1

Table of Contents

billion in unpaid principal balance (UPB) nine months ended September 30, 2016, partially offset by MSR sales of approximately \$815.0 million in UPB. With the decrease in mortgage interest rates and resulting decline in MSR values, instead of selling MSRs at depressed pricing levels, we changed our strategy to retain our servicing and recapture portfolio runoff. During the third quarter of 2016, prepayments increased to \$1.1 billion in UPB as compared to \$881.4 million in UPB in the second quarter. However, during the third quarter, we successfully recaptured and refinanced 85% of these prepayments, an improvement over a 83% retention rate for the second quarter of 2016.

The loss on mortgage servicing rights was primarily due to charges associated with the retention of servicing, as shown below:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2016	2015	2016	2015
Change in fair value of mortgage servicing rights	\$ (8,224)	\$ (4,347)	\$ (32,048)	\$ (7,983)
Loss on sale of mortgage servicing rights	(7,532)	(471)	(10,610)	(6,193)
Realized and unrealized (losses) gains from hedging instruments	(101)	—	1,409	—
Loss on mortgage servicing rights	\$ (15,857)	\$ (4,818)	\$ (41,249)	\$ (14,176)

In the third quarter of 2016, we recorded \$8.2 million in change in fair value of mortgage servicing rights including \$9.4 million in MSR MTM losses due to these prepayments offset by a MTM gain at September 30, 2016 of \$1.2 million. Upon refinancing a borrower in our portfolio, the associated MSR of the initial loan is written off in the form of a mark-to-market (MTM) loss from the prepayment of the loan. However, we also record the origination income from the refinanced loan and the gain on sale including the capitalized servicing value of the new MSR.

During the third quarter, we were successful in negotiating an amendment to a previous MSR sale, extending the early prepayment protection, in return allowing the Company to solicit our borrower for refinance. Under the agreement, the Company agreed to extend the prepayment protection terms and to reimburse the investor up to 100% of the price paid by the investor for the mortgage servicing rights for any loans in the previously sold pools that paid off in full. Upon refinancing a borrower from the sold portfolio, we earn the origination income on the new loans and gain on sale including the capitalized servicing value of the new MSR. In accordance with GAAP, a charge for the current period activity is recorded plus an estimate of all expected servicing premium to be paid to the investor is required to be recorded. In the third quarter of 2016, the loss on mortgage servicing rights of \$7.5 million includes a \$2.8 million charge for third quarter 2016 activity and the remaining balance is primarily related to a reserve for potential future estimated premium recapture charges. As long as the interest rate environment allows for recapture opportunities, we expect to continue to refinance borrowers in the sold portfolio. However, we will monitor the profitability of this extended early prepayment protection on a month-to-month basis. The amendment gives the Company the option to terminate the agreement with a 90 day notification.

The loss on mortgage servicing rights in the third quarter of 2016 were predominantly due to retention efforts resulting in additional origination volume which contributed to the total \$4.2 billion in originations and \$113.2 million in gain on sale of loans, net for the third quarter.

The following table includes information about our mortgage servicing portfolio:

Edgar Filing: IMPAC MORTGAGE HOLDINGS INC - Form 10-Q

(in millions)	At September 30, 2016	% 60+ days delinquent (1)		At December 31, 2015	% 60+ days delinquent (1)	
Fannie Mae	\$ 4,798.6	0.12	%	\$ 1,970.4	0.27	%
Freddie Mac	3,512.8	0.09	%	829.4	0.21	%
Ginnie Mae	948.5	1.30	%	675.7	1.06	%
Other	190.8	0.00	%	95.2	0.00	%
Total servicing portfolio	\$ 9,450.7	0.25	%	\$ 3,570.7	0.43	%

(1) Based on loan count.

41

Table of Contents

In recent quarters, we strategically changed direction to hold higher amounts of MSR's on the balance sheet by focusing on recapturing the runoff in the low interest rate environment. With a successful retention program, we have more options to not only retain MSR's, but also to opportunistically sell certain portions of our servicing portfolio. We believe this to be a successful strategy for us and our overall financial performance, even if and when interest rates move higher. With a strong retention capability, we are able to both take advantage of a low interest rate environment with stronger origination volume, and create a low weighted average coupon portfolio that will increase in value during a rising rate environment. Additionally, we are in negotiations on a MSR financing facility that will assist us in financing the retention of MSR's. We expect this facility to be operational within the next few months.

Our warehouse lending division, whereby we lend funds to other mortgage originators to assist them in closing mortgage loans, continues to grow and the outstanding balance of finance receivables, representing warehouse lending advances to our warehouse customers, increased to \$78.7 million at September 30, 2016 as compared to \$36.4 million at December 31, 2015. Fundings from the warehouse lending division increased to \$286.9 million for the three months ended September 30, 2016 as compared to \$234.6 million for the three months ended June 30, 2016. As of September 30, 2016, the warehouse lending operations had extended warehouse lines to non-affiliated customers totaling \$156.5 million as compared to \$119.5 million at December 31, 2015.

For the third quarter of 2016, real estate services fees were \$2.7 million as compared to \$2.0 million in the second quarter of 2016 and \$2.8 million in the third quarter of 2015. Although the real estate services fees were increased as compared to the second quarter of 2016, we expect these fees to decrease over time with the anticipated runoff of our long-term mortgage portfolio.

In our long-term mortgage portfolio, the residual interests generated cash flows of \$1.6 million in the third quarter of 2016 as compared to \$2.5 million in the second quarter of 2016 and \$1.1 million in the third quarter of 2015. The estimated fair value of the residual interests increased \$2.0 million in the third quarter of 2016 to \$18.1 million at September 30, 2016, as a result of a reduction in forward LIBOR as well as an improvement in performance from certain trusts partially offset by residual cash flows received.

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

Liquidity and Capital Resources

During the nine months ended September 30, 2016, we funded our operations primarily from mortgage lending revenues and to a lesser extent real estate services fees and cash flows from our residual interests in securitizations. Mortgage lending revenues include gains on sale of loans, net, and other mortgage related income, and real estate services fees include portfolio loss mitigation fees primarily generated from our long-term mortgage portfolio. During the nine months ended September 30, 2016, we also received proceeds from the issuance of common stock by raising capital, initiating an equity offering program (EOP) and the conversion of Notes, as further described below. Additionally, we funded mortgage loan originations using warehouse facilities which are repaid once the loan is sold. We may continue to manage our capital through the sale of mortgage servicing rights. We may also seek to raise capital by issuing debt or equity, including offering shares through the EOP.

In September 2016, we entered into an underwriting agreement (Underwriting Agreement) with JMP Securities LLC (Underwriter) pursuant to which we sold 3,000,000 shares of common stock, \$0.01 par value per share, at a public offering price of \$13.00 per share. In addition, under the terms of the Underwriting Agreement, the Underwriter exercised its right to purchase an additional 450,000 shares of common stock. The shares were sold pursuant to a prospectus, dated May 28, 2015, and a prospectus supplement, dated September 15, 2016, in connection with a takedown from our shelf registration statement on Form S-3 (File No. 333-204513) (Registration Statement), declared

effective by the U.S. Securities and Exchange Commission (SEC) on June 16, 2015.

The net proceeds from the offering were approximately \$42.6 million after deducting underwriting discounts and commissions and estimated aggregate offering expenses of \$200 thousand. We intend to use the net proceeds from the offering for general corporate purpose, including working capital and development costs, such as retention of

Table of Contents

servicing on new originations and to grow market share and geographic scope within the CashCall Mortgage retail channel, as well as continued growth in the correspondent and wholesale lending channels.

During the first nine months of 2016, we paid approximately \$28.0 million in contingent consideration payments related to the CCM acquisition payments for the fourth quarter of 2015 and first and second quarter of 2016 earn-out periods. Additionally, the contingent consideration payment for the third quarter of 2016 is approximately \$27.8 million and is due in November 2016. These contingent consideration payments are based on the performance of the CCM division and over time decline for the remaining earn-out periods since the earn-out percentage decreases to 55% of CCM division earnings, as defined, beginning in 2016 and to 45% beginning in 2017.

In January 2016, pursuant to the terms of the \$20.0 million Convertible Promissory Notes issued in April 2013 (the Notes), we elected to exercise our option to convert the Notes to common stock. The conversion resulted in the issuance of 1,839,080 shares of common stock and annual interest expense savings of \$1.5 million. As a result of the transaction, we converted \$20.0 million of debt into equity and were required to pay interest through April 2016 as part of the original agreement. We entered into an agreement with the noteholders to delay the \$125 thousand interest payment until April 2016, which was the original due date, instead of on the date of conversion. The interest owed through April 2016, as well as the remaining debt issuance costs of \$129 thousand were recorded as an expense during the quarter ended March 31, 2016.

On December 3, 2015, we initiated an EOP by filing with the SEC a prospectus supplement under our shelf registration. The EOP allows us to offer and sell, from time to time, up to \$25.0 million of our common stock in negotiated transactions or transactions through the at-the-market-offering, as defined in Rule 415 under the Securities Act of 1933, as amended, including sales made directly on the NYSE MKT or sales made to or through a market maker other than on an exchange. During the three and September 30, 2016, we issued 6,009 and 361,429 shares of our common stock through the EOP at an average price of \$17.53 and \$14.05 per share, respectively. These sales generated proceeds of \$103 thousand and \$5.0 million for the three and nine months ended September 30, 2016, respectively, net of \$2 thousand and \$102 thousand in sales commission, respectively. Under the current EOP, we are now eligible to sell up to an additional \$20.0 million of common stock.

We established the EOP to have the opportunity to raise capital in a way that we believe will mitigate downward pressure on the stock price and add capital in an accretive manner to existing shareholders. In the first nine months of 2016, we issued shares at an average price above the book value per share. We plan to continue to utilize the EOP to support selective retention of MSRs, improve our cost of funds as well as support any acquisition opportunities that may present themselves.

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

We believe that current cash balances, cash flows from our mortgage lending operations, the sale of mortgage servicing rights, real estate services fees generated from our long-term mortgage portfolio, and residual interest cash flows from our long-term mortgage portfolio are adequate for our current operating needs. We believe the mortgage and real estate services market is volatile, highly competitive and subject to increased regulation. Competition in

mortgage lending comes primarily from mortgage bankers, commercial banks, credit unions and other finance companies which operate in our market area as well as throughout the United States. We compete for loans principally on the basis of the interest rates and loan fees we charge, the types of loans we originate and the quality of services we provide to borrowers, brokers and sellers. Additionally, competition for loss mitigation servicing, loan modification services and other portfolio services has increased. Our competitors include mega mortgage servicers, established subprime loan servicers, and newer entrants to the specialty servicing and recovery collections business. Efforts to market our ability to

Table of Contents

provide mortgage and real estate services for others is more difficult than many of our competitors because we have not historically provided such services to unrelated third parties, and we are not a rated primary or special servicer of residential mortgage loans as designated by a rating agency. Additionally, performance of the long-term mortgage portfolio is subject to the current real estate market and economic conditions. Cash flows from our residual interests in securitizations are sensitive to delinquencies, defaults and credit losses associated with the securitized loans. Losses in excess of current estimates will reduce the residual interest cash receipts from our long-term mortgage portfolio.

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

Critical Accounting Policies

We define critical accounting policies as those that are important to the portrayal of our financial condition and results of operations. Our critical accounting policies require management to make difficult and complex judgments that rely on estimates about the effect of matters that are inherently uncertain due to the effect of changing market conditions and/or consumer behavior. In determining which accounting policies meet this definition, we considered our policies with respect to the valuation of our assets and liabilities and estimates and assumptions used in determining those valuations. We believe the most critical accounting issues that require the most complex and difficult judgments and that are particularly susceptible to significant change to our financial condition and results of operations include those issues included in Management's Discussion and Analysis of Results of Operations in IMH's report on Form 10-K for the year ended December 31, 2015. Such policies have not changed during 2016.

Table of Contents

Financial Condition and Results of Operations

Financial Condition

As of September 30, 2016 compared to December 31, 2015

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

	September 30, 2016 (Unaudited)	December 31, 2015	Increase (Decrease)	% Change	
ASSETS					
Cash	\$ 58,902	\$ 32,409	\$ 26,493	82	%
Restricted cash	9,928	3,474	6,454	186	
Mortgage loans held-for-sale	849,521	310,191	539,330	174	
Finance receivables	78,653	36,368	42,285	116	
Mortgage servicing rights	87,413	36,425	50,988	140	
Securitized mortgage trust assets	4,169,519	4,594,534	(425,015)	(9)	
Goodwill	104,938	104,938	—	0	
Intangibles	26,827	29,975	(3,148)	(11)	
Deferred tax asset	24,420	24,420	—	0	
Other assets	49,712	38,118	11,594	30	
Total assets	\$ 5,459,833	\$ 5,210,852	\$ 248,981	5	%
LIABILITIES & EQUITY					
Warehouse borrowings	\$ 880,111	\$ 325,616	\$ 554,495	170	%
Term financing	29,871	29,716	155	1	
Convertible notes	24,962	44,819	(19,857)	(44)	
Long-term debt (\$71,120 par)	39,835	31,898	7,937	25	
Repurchase reserve	6,134	5,236	898	17	
Securitized mortgage trust liabilities	4,151,389	4,580,326	(428,937)	(9)	
Contingent consideration	59,896	48,079	11,817	25	
Other liabilities	53,954	30,672	23,282	76	
Total liabilities	5,246,152	5,096,362	149,790	3	
Total equity	213,681	114,490	99,191	87	
Total liabilities and stockholders' equity	\$ 5,459,833	\$ 5,210,852	\$ 248,981	5	%

During the nine months ended, cash balances increased primarily due to the aforementioned follow-on stock offering with net proceeds of approximately \$42.6 million partially offset by \$28.0 million in contingent consideration payments related to the acquisition of CCM.

Loans held-for-sale (LHFS) increased \$539.3 million to \$849.5 million at September 30, 2016 as compared to \$310.2 million at December 31, 2015. The increase was due to \$9.8 billion in originations during the first nine months of 2016 partially offset by \$9.3 billion in loan sales. As a normal course of our origination and sales cycle, loans held-for-sale at the end of any period are generally sold within one or two subsequent months.

Finance receivables increased \$42.3 million to \$78.7 million at September 30, 2016 as compared to \$36.4 million at December 31, 2015. The increase was due to \$672.9 million in fundings offset by \$630.6 million in settlements.

MSRs increased \$51.0 million to \$87.4 million at September 30, 2016 as compared to \$36.4 million at December 31, 2015. The increase was due to servicing retained loan sales of \$9.1 billion in UPB. Partially offsetting the increase was a bulk sale of MSRs totaling approximately \$815.0 million in UPB and a mark-to-market reduction in fair value of \$32.0 million. At September 30, 2016, we serviced \$9.5 billion in UPB for others as compared to \$3.6 billion at December 31, 2015.

45

Table of Contents

Warehouse borrowings increased \$554.5 million to \$880.1 million at September 30, 2016 as compared to \$325.6 million at December 31, 2015. The increase was due to an increase in LHFS attributable to the increased loan volume and increased finance receivables at September 30, 2016. During September 30, 2016, we increased our total borrowing capacity to \$1.0 billion as compared to \$675.0 million at December 31, 2015.

Convertible notes decreased \$19.9 million to \$25.0 million at September 30, 2016 as compared to \$44.8 million at December 31, 2015. In January 2016, we elected to exercise our option to convert the \$20.0 million in Notes to common stock. As a result, we converted \$20.0 million of debt into equity by issuing an aggregate of 1,839,080 shares of common stock.

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

	September 30, 2016	December 31, 2015	Increase (Decrease)	% Change	
Securitized mortgage collateral	\$ 4,155,457	\$ 4,574,919	\$ (419,462)	(9)	%
Other trust assets	14,062	19,615	(5,553)	(28)	
Total trust assets	4,169,519	4,594,534	(425,015)	(9)	
Securitized mortgage borrowings	\$ 4,151,365	\$ 4,578,657	\$ (427,292)	(9)	%
Other trust liabilities	24	1,669	(1,645)	(99)	
Total trust liabilities	4,151,389	4,580,326	(428,937)	(9)	
Residual interests in securitizations	\$ 18,130	\$ 14,208	\$ 3,922	28	%

Since the consolidated and unconsolidated securitization trusts are nonrecourse to us, trust assets and liabilities have been netted to present our interest in these trusts more simply, which are considered the residual interests in securitizations. For unconsolidated securitizations the residual interests represent the fair value of investment securities available-for-sale. For consolidated securitizations, the residual interests are represented by the fair value of securitized mortgage collateral and real estate owned, offset by the fair value of securitized mortgage borrowings and derivative liabilities. We receive cash flows from our residual interests in securitizations to the extent they are available after required distributions to bondholders and maintaining specified overcollateralization levels and other specified parameters (such as maximum delinquency and cumulative default) within the trusts. The estimated fair value of the residual interests, represented by the difference in the fair value of total trust assets and total trust liabilities, was \$18.1 million at September 30, 2016 compared to \$14.2 million at December 31, 2015.

We update our collateral assumptions quarterly based on recent delinquency, default, prepayment and loss experience. Additionally, we update the forward interest rates and investor yield (discount rate) assumptions based on information derived from market participants. During the nine months ended September 30, 2016, actual losses were relatively flat and were inline with forecasted losses for the majority of trusts with residual value. Principal payments and liquidations of securitized mortgage collateral and securitized mortgage borrowings also contributed to the reduction in trust assets and liabilities. Offsetting the decrease in securitized mortgage collateral and securitized mortgage borrowings was a decrease in forward LIBOR as compared to December 31, 2015. The decrease in loss assumptions on certain trusts with residual value and decrease in the forward LIBOR curve resulted in an increase in the value of our residual interests at September 30, 2016.

· The estimated fair value of securitized mortgage collateral decreased \$419.5 million during the nine months ended September 30, 2016, primarily due to reductions in principal from borrower payments and transfers of loans

to Real Estate Owned (REO) for single-family and multi-family collateral. Additionally, other trust assets decreased \$5.6 million during the nine months ended September 30, 2016, primarily due to liquidations of \$32.3 million and a \$6.0 million decrease in the net realizable value (NRV) of REO. Partially offsetting the decrease was an increase of \$32.7 million in REO from foreclosures.

- The estimated fair value of securitized mortgage borrowings decreased \$427.3 million during the nine months ended September 30, 2016, primarily due to reductions in principal balances from principal

Table of Contents

payments during the period for single-family and multi-family collateral as well as a decrease in loss assumptions. The \$1.6 million reduction in other trust liabilities during the nine months ended September 30, 2016, was primarily due to \$1.7 million in derivative cash payments from the securitization trusts, and a \$199 thousand increase in derivative fair value resulting from changes in forward LIBOR interest rates.

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

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

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

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

Table of Contents

The following table presents changes in the trust assets and trust liabilities for the nine months ended September 30, 2016:

	TRUST ASSETS				TRUST LIABILITIES			Net trust assets
	Level 3 Recurring Fair Value Measurements Investment securities available-for-sale	Securitized mortgage collateral	NRV (1) Real estate owned	Total trust assets	Level 3 Recurring Fair Value Measurements Securitized mortgage borrowings	Derivative liabilities	Total trust liabilities	
Recorded book value at September 30, 2015	\$ 26	\$ 4,574,919	\$ 19,589	\$ 4,594,534	\$ (4,578,657)	\$ (1,669)	\$ (4,580,326)	\$ 14,208
Changes:								
Interest income	2	46,540	—	46,542	—	—	—	46,542
Interest expense	—	—	—	—	(141,927)	—	(141,927)	(141,927)
Change in FV of net trust assets, including REO (2)	19	27,780	—	27,799	(19,020)	(199)	(19,219)	8,580
Losses from REO – at FV but at NRV (2)	—	—	(5,971)	(5,971)	—	—	—	(5,971)
Net gains (losses) included in earnings transfers in and/or out of level 3	21	74,320	(5,971)	68,370	(160,947)	(199)	(161,146)	(92,776)
Acquisitions, issuances and settlements	(47)	(493,782)	444	(493,385)	588,239	1,844	590,083	96,698
Recorded book value at September 30, 2016	\$ —	\$ 4,155,457	\$ 14,062	\$ 4,169,519	\$ (4,151,365)	\$ (24)	\$ (4,151,389)	\$ 18,130

(1) Accounted for at net realizable value.

(2) Represents change in fair value of net trust assets, including trust REO (losses) gains in the consolidated statements of operations for the nine months ended September 30, 2016.

Inclusive of losses from REO, total trust assets above reflect a net gain of \$21.8 million for the nine months ended September 30, 2016 as a result of an increase in fair value from securitized mortgage collateral and other trust assets of \$27.8 million and \$19 thousand, respectively, offset by losses from REO of \$6.0 million. Net losses on trust liabilities were \$19.2 million as a result of \$19.0 million in losses from the increase in fair value of securitized mortgage borrowings and losses from derivative liabilities of \$199 thousand. As a result, non-interest income—net trust assets totaled an increase of \$2.6 million for the nine months ended September 30, 2016.

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

September 30, December 31,

Edgar Filing: IMPAC MORTGAGE HOLDINGS INC - Form 10-Q

	2016		2015	
Net trust assets	\$ 18,130		\$ 14,208	
Total trust assets	4,169,519		4,594,534	
Net trust assets as a percentage of total trust assets	0.43	%	0.31	%

For the nine months ended September 30, 2016, the estimated fair value of the net trust assets increased as a percentage of total trust assets. The increase was primarily due to an increase in projected future cash flows due to a decrease in loss assumptions in the 2006 multi-family vintage as well as a decrease in forward LIBOR.

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

Table of Contents

The following tables present the estimated fair value of our residual interests, including investment securities available for sale, by securitization vintage year and other related assumptions used to derive these values at September 30, 2016 and December 31, 2015:

Origination Year	Estimated Fair Value of Residual Interests by Vintage Year at September 30, 2016			Estimated Fair Value of Residual Interests by Vintage Year at December 31, 2015		
	SF	MF	Total	SF	MF	Total
2002-2003 (1)	\$ 8,057	\$ 925	\$ 8,982	\$ 9,410	\$ 1,401	\$ 10,811
2004	1,612	838	2,450	1,198	805	2,003
2005	39	1	40	213	29	242
2006	—	6,658	6,658	—	1,152	1,152
Total	\$ 9,708	\$ 8,422	\$ 18,130	\$ 10,821	\$ 3,387	\$ 14,208
Weighted avg. prepayment rate	6.6 %	11.4 %	6.9 %	5.6 %	8.1 %	5.8 %
Weighted avg. discount rate	16.7 %	18.3 %	17.5 %	16.3 %	14.7 %	15.9 %

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

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

The table below reflects the estimated future credit losses and investor yield requirements for trust assets by product (SF and MF) and securitization vintage at September 30, 2016:

	Estimated Future Losses (1)			Investor Yield Requirement (2)		
	SF	MF		SF	MF	
2002-2003	9 %	*	(3)	5 %	7 %	
2004	8	*	(3)	5	5	
2005	12	6 %		5	3	
2006	20	2		6	5	
2007	17	4		7	3	

(1) Estimated future losses derived by dividing future projected losses by UPB at September 30, 2016.

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

(3) Represents less than 1%.

Despite the increase in housing prices through September 30, 2016, housing prices in many parts of the country are

still at levels which have significantly reduced or eliminated equity for loans originated after 2003. Future loss estimates are significantly higher for mortgage loans included in securitization vintages after 2005 which reflect severe home price deterioration and defaults experienced with mortgages originated during these periods.

Long-Term Mortgage Portfolio Credit Quality

49

Table of Contents

We use the Mortgage Bankers Association (MBA) method to define delinquency as a contractually required payment being 30 or more days past due. We measure delinquencies from the date of the last payment due date in which a payment was received. Delinquencies for loans 60 days delinquent or greater, foreclosures and delinquent bankruptcies were \$1.0 billion or 19.1% of the long-term mortgage portfolio as of September 30, 2016. Despite the increase in percentage of loans 60 or more days delinquent at September 30, 2016 as compared to December 31, 2015, the UPB of loans 60 days or more delinquent at September 30, 2016 decreased by \$111.9 million.

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

	September 30, 2016	Total Collateral		December 31, 2015	Total Collateral
Securitized mortgage collateral					
60 - 89 days delinquent	\$ 98,376	1.9	%	\$ 125,937	2.1 %
90 or more days delinquent	440,429	8.3		394,129	6.7
Foreclosures (1)	245,772	4.6		351,276	6.0
Delinquent bankruptcies (2)	224,076	4.2		249,225	4.2
Total 60 or more days delinquent	\$ 1,008,653	19.1		\$ 1,120,567	19.0
Total collateral	\$ 5,289,770	100.0		\$ 5,900,239	100.0

(1) Represents properties in the process of foreclosure.

(2) Represents bankruptcies that are 30 days or more delinquent.

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

	September 30, 2016	Total Collateral %		December 31, 2015	Total Collateral %
90 or more days delinquent, foreclosures and delinquent bankruptcies	\$ 910,277	17.2	%	\$ 994,630	16.9 %
Real estate owned	14,062	0.3		19,589	0.3
Total non-performing assets	\$ 924,339	17.5		\$ 1,014,219	17.2

Non-performing assets consist of non-performing loans (mortgages that are 90 or more days delinquent, including loans in foreclosure and delinquent bankruptcies) plus REO. It is our policy to place a mortgage on nonaccrual status when it becomes 90 days delinquent and to reverse from revenue any accrued interest, except for interest income on securitized mortgage collateral when the scheduled payment is received from the servicer. The servicers are required to advance principal and interest on loans within the securitization trusts to the extent the advances are considered recoverable. IFC, a subsidiary of IMH and master servicer, may be required to advance funds, or in most cases cause the loan servicers to advance funds, to cover principal and interest payments not received from borrowers depending on the status of their mortgages. As of September 30, 2016, non-performing assets (UPB of loans 90 or more days delinquent, foreclosures and delinquent bankruptcies plus REO) as a percentage of the total collateral was 17.5%. At December 31, 2015, non-performing assets to total collateral was 17.2%. Non-performing assets decreased by approximately \$89.9 million at September 30, 2016 as compared to December 31, 2015. At September 30, 2016, the estimated fair value of non-performing assets (representing the fair value of loans 90 or more days delinquent, foreclosures and delinquent bankruptcies plus REO) was \$285.2 million or 5.2% of total assets. At December 31, 2015, the estimated fair value of non-performing assets was \$388.6 million or 7.5% of total assets.

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

50

Table of Contents

For the three and nine months ended September 30, 2016, we recorded a decrease in net realizable value of the REO in the amount of \$1.4 million and \$6.0 million, respectively, compared to a decrease of \$2.4 million and \$4.9 million for the comparable 2015 period. Increases and write-downs of the net realizable value reflect increases or declines in value of the REO subsequent to foreclosure date, but prior to the date of sale.

The following table presents the balances of REO:

	September 30, 2016	December 31, 2015
REO	\$ 28,502	\$ 28,058
Impairment (1)	(14,440)	(8,469)
Ending balance	\$ 14,062	\$ 19,589
REO inside trusts	\$ 14,062	\$ 19,589
REO outside trusts	—	—
Total	\$ 14,062	\$ 19,589

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

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

Table of Contents

Results of Operations

For the Three Months Ended September 30, 2016 compared to the Three Months Ended September 30, 2015

	For the Three Months Ended September 30,			
	2016	2015	Increase (Decrease)	% Change
Revenues	\$ 103,993	\$ 47,652	\$ 56,341	118 %
Expenses (1)	(81,359)	(24,677)	(56,682)	(230)
Net interest income	1,304	119	1,185	996
Change in fair value of long-term debt	(8,641)	—	(8,641)	n/a
Change in fair value of net trust assets, including trust				
REO gains	1,071	(3,004)	4,075	136
Income tax benefit (expense)	130	(781)	911	117
Net earnings	\$ 16,498	\$ 19,309	\$ (2,811)	(15)
Earnings per share available to common stockholders—basic	\$ 1.28	\$ 1.89	\$ (0.61)	(32) %
Earnings per share available to common stockholders—diluted	\$ 1.18	\$ 1.48	\$ (0.30)	(21) %

(1) Includes changes in contingent consideration liability resulting in expense of \$23.2 million for the three months ended September 30, 2016 and income of \$16.9 million for the three months ended September 30, 2015.

	For the Nine Months Ended September 30,			
	2016	2015	Increase (Decrease)	% Change
Revenues	\$ 220,506	\$ 131,080	\$ 89,426	68 %
Expenses (1)	(187,408)	(74,238)	(113,170)	(152)
Net interest income	2,036	2,135	(99)	(5)
Change in fair value of long-term debt	(7,286)	(8,661)	1,375	16
Change in fair value of net trust assets, including trust				
REO gains (losses)	2,609	(3,078)	5,687	185
Income tax (expense) benefit	(728)	22,852	(23,580)	(103)
Net earnings	\$ 29,729	\$ 70,090	\$ (40,361)	(58)
Earnings per share available to common stockholders—basic	\$ 2.43	\$ 7.00	\$ (4.57)	(65) %
Earnings per share available to common stockholders—diluted	\$ 2.27	\$ 5.61	\$ (3.34)	(59) %

(1) Includes changes in contingent consideration liability resulting in expense of \$34.6 million for the nine months ended September 30, 2016 and income of \$28.2 million for the nine months ended September 30, 2015.

Revenues

For the Three Months Ended September 30,
Increase %

Edgar Filing: IMPAC MORTGAGE HOLDINGS INC - Form 10-Q

	2016	2015	(Decrease)	Change	
Gain on sale of loans, net	\$ 113,158	\$ 47,274	\$ 65,884	139	%
Real estate services fees, net	2,678	2,775	(97)	(3)	
Servicing income, net	3,789	2,432	1,357	56	
Loss on mortgage servicing rights	(15,857)	(4,818)	(11,039)	(229)	
Other revenues	225	(11)	236	2145	
Total revenues	\$ 103,993	\$ 47,652	\$ 56,341	118	%

Gain on sale of loans, net. For the three months ended September 30, 2016, gain on sale of loans, net were \$113.2 million compared to \$47.3 million in the comparable 2015 period. The \$65.9 million increase is primarily due to

52

Table of Contents

a \$49.3 million increase in premiums from the sale of mortgage loans, a \$17.5 million increase in premiums from servicing retained loan sales and a \$8.5 million increase in realized and unrealized net gains on derivative financial instruments, partially offset by a \$7.2 million increase in direct loan origination expenses, a \$1.4 million decrease in mark-to-market gains, and a \$907 thousand decrease in provision for repurchases.

The overall increase in gain on sale of loans, net was primarily due to increased volumes and gain on sale margins. For the three months ended September 30, 2016, we originated and sold \$4.2 billion and \$4.1 billion of loans, respectively, as compared to \$2.3 billion and \$2.2 billion of loans originated and sold, respectively, during the same period in 2015. Margins increased to approximately 268 bps for the three months ended September 30, 2016 as compared to 205 bps for the same period in 2015 due to a higher concentration of retail loans which have higher margins.

Real estate services fees, net. For the three months ended September 30, 2016, real estate services fees, net were \$2.7 million compared to \$2.8 million in the comparable 2015 period. The \$97 thousand decrease was primarily the result of a decrease in transactions related to the decline in the number of loans and the UPB of the long-term mortgage portfolio as compared to the third quarter of 2015.

Servicing income, net. For the three months ended September 30, 2016, servicing income, net was \$3.8 million compared to \$2.4 million in the comparable 2015 period. The increase in servicing income, net was the result of the servicing portfolio increasing 59% to an average balance of \$8.5 billion for the three months ended September 30, 2016 as compared to an average balance of \$5.4 billion for the three months ended September 30, 2015. The increase in the average balance of the servicing portfolio is a result of servicing retained loan sales of \$4.0 billion during the three months ended September 30, 2016

Loss on mortgage servicing rights. For the three months ended September 30, 2016, loss on MSR was \$15.9 million compared to \$4.8 million in the comparable 2015 period. For the three months ended September 30, 2016, we recorded an \$8.2 million loss from change in fair value of MSR including \$9.4 million in mark-to-market (MTM) losses due to \$1.1 billion UPB of prepayments offset by a MTM gain at September 30, 2016 of \$1.2 million due to a slight increase in mortgage interest rates in September. As a result of our successful retention efforts, we recaptured and refinanced 85% of these prepayments at a lower coupon rate and thus a higher servicing value. Despite the MTM loss from loan prepayments recorded as a loss on MSR, there was also a corresponding income from the recaptured loan with a higher MSR value recognized in gain on sale of loans, net in the consolidated statement of operations.

In addition to the MTM loss on MSR, during the three months ended September 30, 2016 we had a \$7.5 million loss on sale of MSR related to refunds of premiums to investors for loan payoffs associated with sales of servicing rights in previous periods as compared to \$471 thousand in the comparable 2015 period. During the third quarter of 2016, we amended a previous MSR sale agreement, extending the early prepayment protection, in return allowing the Company to solicit the sold portfolio. In the third quarter of 2016, the loss on mortgage servicing rights of \$7.5 million includes a \$2.8 million charge for third quarter 2016 activity and the remaining balance is primarily related to a reserve for potential future estimated premium recapture charges. As long as the interest rate environment allows for recapture opportunities, we expect to continue to refinance borrowers in the sold portfolio. However, we will monitor the profitability of this extended early prepayment protection on a month-to-month basis. The amendment gives the Company the option to terminate the agreement with a 90 day notification.

Table of Contents

	For the Nine Months Ended September 30,			
	2016	2015	Increase (Decrease)	% Change
Gain on sale of loans, net	\$ 245,849	\$ 133,018	\$ 112,831	85 %
Real estate services fees, net	6,773	7,872	(1,099)	(14)
Servicing income, net	8,680	4,083	4,597	113
Loss on mortgage servicing rights	(41,249)	(14,176)	(27,073)	(191)
Other revenues	453	283	170	60
Total revenues	\$ 220,506	\$ 131,080	\$ 89,426	68 %

Gain on sale of loans, net. Gain on sale of loans, net includes the operating expenses of CCM in the first quarter of 2015 before we closed the transaction on March 31, 2015. We received the economic benefit of the CCM transactions from the beginning of 2015 but did not hire the employees of CCM or incur direct operating expenditures of CCM until after the close of the transaction. Accordingly, operating expenses for CCM in the first quarter of 2015 were included within gain on sale of loans, net as loan origination costs in the consolidated statements of operations. Beginning with the second quarter of 2015 the operating expenses of CCM were included in personnel, business promotion, general, administrative and other expense, as normally presented.

For the nine months ended September 30, 2016, gain on sale of loans, net were \$245.8 million compared to \$133.0 million in the comparable 2015 period. The \$112.8 million increase is primarily due to \$9.8 billion in originations for the nine months ended September 30, 2016 as compared to \$7.3 billion for the same period in 2015 as well as the presentation of CCM operating expenses in the first quarter of 2015.

Real estate services fees, net. For the nine months ended September 30, 2016, real estate services fees, net were \$6.8 million compared to \$7.9 million in the comparable 2015 period. The \$1.1 million decrease was primarily the result of a decrease in transactions related to the decline in the number of loans and the UPB of the long-term mortgage portfolio as compared to the first nine months of 2015.

Servicing income, net. For the nine months ended September 30, 2016, servicing income, net was \$8.7 million compared to \$4.1 million in the comparable 2015 period. The increase in servicing income, net was the result of the servicing portfolio increasing 78% to an average balance of \$6.4 billion for the nine months ended September 30, 2016 as compared to an average balance of \$3.6 billion for the nine months ended September 30, 2015. The increase in the average balance of the servicing portfolio is a result of servicing retained loan sales of \$9.1 billion during the nine months ended September 30, 2016 partially offset by a bulk sale of MSR's of approximately \$815.0 million.

Loss on mortgage servicing rights. For the nine months ended September 30, 2016, loss on MSR's was \$41.2 million compared to \$14.2 million in the comparable 2015 period. For the nine months ended September 30, 2016, we recorded a \$32.0 million loss from a change in fair value of MSR's primarily the result of \$2.4 billion in prepayments due to the low mortgage interest rate environment during the first nine months of 2016 which resulted in an increase in actual prepayments as well as prepayment speed assumptions. For the nine months ended September 30, 2016, as a result of our successful retention efforts, we recaptured and refinanced 83% of these prepayments at a lower coupon rate and thus a higher servicing value. Despite the MTM loss from loan prepayments recorded as a loss on MSR's, there was also a corresponding income from the recaptured loan with a higher MSR value recognized in gain on sale of loans, net in the consolidated statement of operations.

In addition to the MTM loss on MSRs, during the nine months ended September 30, 2016 we had a \$10.6 million loss on sale of mortgage servicing rights related to refunds of premiums to investors for loan payoffs associated with sales of servicing rights in previous periods as compared to \$6.2 million in the comparable 2015 period as well a \$1.0 million loss on the sale of \$815.0 million UPB of MSRs. Partially offsetting the loss was a \$1.4 million increase in realized and unrealized gains from hedging instruments related to MSRs. During the third quarter of 2016, we amended a previous MSR sale agreement, extending the early prepayment protection, in return allowing the Company to solicit the sold portfolio. In the third quarter of 2016, the loss on mortgage servicing rights of \$7.5 million includes a \$2.8 million charge for third quarter 2016 activity and the remaining balance is primarily related to a reserve for potential future estimated premium recapture charges. As long as the interest rate environment allows for recapture opportunities, we expect to continue to refinance borrowers in the sold portfolio. However, we will monitor the profitability of this

Table of Contents

extended early prepayment protection on a month-to-month basis. The amendment gives the Company the option to terminate the agreement with a 90 day notification.

Expenses

	For the Three Months Ended September 30,			
	2016	2015	Increase (Decrease)	% Change
Personnel expense	\$ 38,467	\$ 21,315	\$ 17,152	80 %
Business promotion	10,350	10,735	(385)	(4)
General, administrative and other	7,736	7,100	636	9
Accretion of contingent consideration	1,591	2,424	(833)	(34)
Change in fair value of contingent consideration	23,215	(16,897)	40,112	237
Total expenses	\$ 81,359	\$ 24,677	\$ 56,682	230 %

Total expenses were \$81.4 million for the three months ended September 30, 2016, compared to \$24.7 million for the comparable period of 2015. Personnel expense increased \$17.2 million to \$38.5 million for the three months ended September 30, 2016. The increase is primarily due to an increase in commission expense due to an increase in loan origination volumes as well as an increase in personnel related costs due to the addition of new sales personnel.

Business promotion was \$10.4 million for the three months ended September 30, 2016, compared to \$10.7 million for the comparable period of 2015. Our centralized call center purchases leads and promotes its business through radio and television advertisements. Despite the slight decrease in advertising expense, origination volume increased as we continue to focus on growing market share and geographic scope within the CashCall Mortgage retail channel, as well as continued growth in the correspondent and wholesale lending channels.

Beginning in the second quarter of 2015, as part of the acquisition of CCM, we record accretion of the contingent consideration liability from the close of the transaction in March 2015 through the end of the earn-out period in December 2017, which increases the contingent consideration liability. The estimated contingent consideration liability is based on discounted cash flows which represent the time value of money of the liability during the earn-out period. In the third quarter of 2016, accretion increased the contingent consideration liability by \$1.6 million as compared to \$2.4 million during the third quarter of 2015. The reduction in accretion is due to the reduction in the estimated future pre-tax earnings as compared to projections in 2015. The accretion will continue to be a charge against earnings in future quarters until the end of the earn-out period.

We recorded a \$23.2 million change in fair value associated with an increase in the contingent consideration liability for the third quarter of 2016 related to updated assumptions including current market conditions and increased mortgage loan originations for CCM. The change in fair value of contingent consideration was related to the estimated increase in future pre-tax earnings of CCM over the remaining earn-out period of five quarters. The fair value of contingent consideration may change from quarter to quarter based upon actual experience and updated assumptions used to forecast pre-tax earnings for CCM. Even though this projected increase in mortgage volume for CCM is favorable, it resulted in a corresponding charge to earnings of \$23.2 million in the third quarter of 2016.

Table of Contents

	For the Nine Months Ended September 30,			
	2016	2015	Increase (Decrease)	% Change
Personnel expense	\$ 93,025	\$ 56,883	\$ 36,142	64 %
Business promotion	30,828	19,628	11,200	57
General, administrative and other	23,742	20,479	3,263	16
Accretion of contingent consideration	5,244	5,471	(227)	(4)
Change in fair value of contingent consideration	34,569	(28,223)	62,792	222
Total expenses	\$ 187,408	\$ 74,238	\$ 113,170	152 %

Total expenses were \$187.4 million for the nine months ended September 30, 2016, compared to \$74.2 million for the comparable period of 2015. The increase in expenses is due to the CCM acquisition and the presentation of CCM operating expenses in the first quarter of 2015 before we closed the transaction on March 31, 2015. We received the economic benefit of the CCM transaction from the beginning of 2015 but did not hire the employees of CCM or incur direct operating expenditures of CCM until the transaction closed on March 31, 2015. Accordingly, operating expenses for CCM in the first quarter of 2015 were included within gain on sale of loans, net as loan origination costs in the consolidated statements of operations. Beginning with the second quarter of 2015 the operating expenses of CCM were included in personnel, business promotion, general, administrative and other expense, as normally presented.

Beginning in the second quarter of 2015, as part of the acquisition of CCM, we record accretion of the contingent consideration liability from the close of the transaction in March 2015 through the end of the earn-out period in December 2017, which increases the contingent consideration liability. The estimated contingent consideration liability is based on discounted cash flows which represent the time value of money of the liability during the earn-out period. In the first nine months of 2016, accretion increased the contingent consideration liability by \$5.2 million. We did not record accretion in the first quarter of 2015 as the acquisition transaction did not close until March 31, 2015, however the accretion will continue to be a charge against earnings in the future five quarters until the end of the earn-out period.

We recorded a \$34.6 million change in fair value associated with an increase in the contingent consideration liability for the first nine months of 2016 related to updated assumptions including current market conditions and increased mortgage loan originations for CCM. The change in fair value of contingent consideration was related to the estimated increase in future pre-tax earnings of CCM over the remaining earn-out period of five quarters. The fair value of contingent consideration may change from quarter to quarter based upon actual experience and updated assumptions used to forecast pre-tax earnings for CCM. Even though this projected increase in mortgage volume for CCM is favorable, it resulted in a corresponding charge to earnings of \$34.6 million in the third quarter of 2016.

Net Interest Income (Expense)

We earn net interest income primarily from mortgage assets, which include securitized mortgage collateral, loans 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. Interest expense is primarily interest paid on borrowings secured by mortgage assets, which include securitized mortgage borrowings and warehouse borrowings and to a lesser extent, interest expense paid on long-term debt, Convertible Notes, short-term borrowings, Term Financing and line of credit. Interest income and interest expense during the period primarily represents the effective yield, based on the fair value of the trust assets and liabilities.

Table of Contents

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

	For the Three Months Ended September 30,					
	2016			2015		
	Average Balance	Interest	Yield	Average Balance	Interest	Yield
ASSETS						
Securitized mortgage collateral	\$ 4,223,226	\$ 59,616	5.65 %	\$ 4,887,919	\$ 66,239	5.42 %
Mortgage loans held-for-sale	494,918	4,606	3.72	357,827	3,558	3.98
Finance receivables	53,868	700	5.20	42,025	495	4.71
Other	15,401	10	0.26	20,303	9	0.18
Total interest-earning assets	\$ 4,787,413	\$ 64,932	5.43	\$ 5,308,074	\$ 70,301	5.30
LIABILITIES						
Securitized mortgage borrowings	\$ 4,219,975	\$ 57,043	5.41	\$ 4,886,775	\$ 64,239	5.26 %
Warehouse borrowings (1)	537,084	4,222	3.14	396,019	3,397	3.43
Long-term debt	35,412	1,078	12.18	31,550	934	11.84
Convertible notes	24,963	469	7.52	45,000	859	7.64
Term financing	29,813	806	10.81	30,000	737	9.83
Other	2,797	10	1.43	2,289	16	2.80
Total interest-bearing liabilities	\$ 4,850,044	\$ 63,628	5.25	\$ 5,391,633	\$ 70,182	5.21
Net Interest Spread (2)		\$ 1,304	0.18 %		\$ 119	0.09 %
Net Interest Margin (3)			0.11 %			0.01 %

(1) Warehouse borrowings include the borrowings from mortgage loans held-for-sale and finance receivables.

(2) Net interest spread is calculated by subtracting the weighted average yield on interest-bearing liabilities from the weighted average yield on interest-earning assets.

(3) Net interest margin is calculated by dividing net interest spread by total average interest-earning assets.

Net interest spread increased \$1.2 million for the quarter ended September 30, 2016 primarily attributable to an increase in the net interest spread on securitized mortgage collateral and securitized mortgage borrowings, an increase in the net interest spread between loans held-for-sale and finance receivables and their related warehouse borrowings and a decrease in interest expense on the convertible debt. The decrease in interest expense from the Convertible Notes is due to the conversion of the Notes in the first quarter of 2016. Offsetting the increase in net spread was a slight increase in interest expense on the long-term debt and term financing. As a result, net interest margin increased to 0.11% for the three months ended September 30, 2016 as compared to 0.01% for the three months ended September 30, 2015.

During the quarter ended September 30, 2016, the yield on interest-earning assets increased to 5.43% from 5.30% in the comparable 2015 period. The yield on interest-bearing liabilities increased to 5.25% for the quarter ended September 30, 2016 from 5.21% for the comparable 2015 period. In connection with the fair value accounting for investment securities available-for-sale, securitized mortgage collateral and borrowings and long-term debt, interest income and interest expense is recognized using effective yields based on estimated fair values for these instruments. The increase in yield for securitized mortgage collateral and securitized mortgage borrowings is primarily related to decreased prices on mortgage-backed bonds which resulted in an increase in yield as compared to the previous period.

Table of Contents

	For the Nine Months Ended September 30,					
	2016			2015		
	Average			Average		
	Balance	Interest	Yield	Balance	Interest	Yield
ASSETS						
Securitized mortgage collateral	\$ 4,346,482	\$ 188,707	5.79 %	\$ 5,034,115	\$ 198,965	5.27 %
Mortgage loans held-for-sale	397,565	11,325	3.80	348,931	9,408	3.59
Finance receivables	37,302	1,502	5.37	59,851	1,773	3.95
Other	21,028	27	0.17	17,285	31	0.24
Total interest-earning assets	\$ 4,802,377	\$ 201,561	5.60	\$ 5,460,182	\$ 210,177	5.13
LIABILITIES						
Securitized mortgage borrowings	\$ 4,346,741	\$ 181,362	5.56 %	\$ 5,032,136	\$ 192,689	5.11 %
Warehouse borrowings (1)	425,882	10,701	3.35	382,603	9,248	3.22
Long-term debt	33,716	3,088	12.21	28,717	2,827	13.13
Convertible notes	24,961	2,050	10.95	33,370	1,918	7.66
Term financing	29,792	2,300	10.29	11,429	847	9.88
Short-term borrowings	—	—	—	4,668	399	11.40
Other	2,461	24	1.30	4,487	114	3.39
Total interest-bearing liabilities	\$ 4,863,553	\$ 199,525	5.47	\$ 5,497,410	\$ 208,042	5.05
Net Interest Spread (2)		\$ 2,036	0.13 %		\$ 2,135	0.08 %
Net Interest Margin (3)			0.06 %			0.05 %

(1) Warehouse borrowings include the borrowings from mortgage loans held-for-sale and finance receivables.

(2) Net interest spread is calculated by subtracting the weighted average yield on interest-bearing liabilities from the weighted average yield on interest-earning assets.

(3) Net interest margin is calculated by dividing net interest spread by total average interest-earning assets.

Net interest spread decreased \$99 thousand for the nine months ended September 30, 2016 primarily attributable to an increase in interest expense from the issuance of the additional Convertible Note in 2015, Term Financing and long-term debt. The increase in interest expense related to the Convertible Notes and Term Financing is partially due to the timing of the transactions as they were entered into in May and June 2015, respectively. Additionally, the Convertible Notes interest expense has an additional \$129 thousand of debt issuance costs accelerated upon conversion in February 2016. Offsetting the decrease in net spread was an increase in the net interest spread on the securitized mortgage collateral and securitized mortgage borrowings, an increase in the net interest spread between loans held-for-sale and finance receivables and their related warehouse borrowings. Despite the decrease in net interest spread, the net interest margin increased to 0.06% for the nine months ended September 30, 2016 from 0.05% for the nine months ended September 30, 2015.

During the nine months ended September 30, 2016, the yield on interest-earning assets increased to 5.60% from 5.13% in the comparable 2016 period. The yield on interest-bearing liabilities increased to 5.47% for the nine months ended September 30, 2016 from 5.05% for the comparable 2015 period. In connection with the fair value accounting for investment securities available-for-sale, securitized mortgage collateral and borrowings and long-term debt, interest income and interest expense is recognized using effective yields based on estimated fair values for these instruments. The increase in yield for securitized mortgage collateral and securitized mortgage borrowings is primarily related to decreased prices on mortgage-backed bonds which resulted in an increase in yield as compared to the previous period.

Change in the fair value of long-term debt.

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

58

Table of Contents

term debt, while deterioration in financial results and financial condition could result in a decrease in the estimated fair value of the long-term debt.

Change in the fair value of long-term debt resulted in an expense of \$8.6 million for the three months ended September 30, 2016, compared to no gain or loss for the comparable 2015 period as a result of an increase in the estimated fair value of long-term debt. The increase in the estimated fair value of long-term debt was primarily the result of a decrease in the discount rate attributable to an improvement in our own credit risk profile associated with our capital raise during the third quarter, improvement in our financial condition and results of operations from the mortgage lending segment during the third quarter of 2016.

Change in the fair value of long-term debt resulted in an expense of \$7.3 million for the nine months ended September 30, 2016, compared to an expense of \$8.7 million for the comparable 2015 period as a result of the increase in the estimated fair value of long-term debt. The increase in the estimated fair value of long-term debt during the September 30, 2016 was primarily the result of a decrease in the discount rate attributable to an improvement in our own credit risk profile associated with our capital raise during the third quarter, improvement in our financial condition and results of operations from the mortgage lending segment during the third quarter of 2016. The increase in the estimated fair value of long-term debt during the 2015 was primarily the result of a decrease in the discount rate attributable to an improvement in our own credit risk profile, improvement in our financial condition and results of operations from the mortgage lending segment including the acquisition of CCM during the first quarter of 2015 as well as an increase in forward LIBOR interest rates during the second quarter of 2015.

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

	For the Three Months Ended September 30, 2016		For the Nine Months Ended September 30, 2015	
	2016	2015	2016	2015
Change in fair value of net trust assets, excluding REO	\$ 2,511	\$ (568)	\$ 8,580	\$ 1,821
Losses from REO	(1,440)	(2,436)	(5,971)	(4,899)
Change in fair value of net trust assets, including trust REO losses	\$ 1,071	\$ (3,004)	\$ 2,609	\$ (3,078)

The change in fair value related to our net trust assets (residual interests in securitizations) was a gain of \$1.1 million for the three months ended September 30, 2016, compared to a loss of \$3.0 million in the comparable 2015 period. The change in fair value of net trust assets, excluding REO was due to \$2.5 million in gains from changes in fair value of securitized mortgage borrowings, securitized mortgage collateral, derivative liabilities and investment securities available-for-sale primarily associated with a decrease in LIBOR as well as updated assumptions on certain later vintage trusts with improved performance. Additionally, the NRV of REO decreased \$1.4 million during the period attributed to higher expected loss severities on properties held in the long-term mortgage portfolio during the period.

The change in fair value related to our net trust assets (residual interests in securitizations) was a gain of \$2.6 million for the nine months ended September 30, 2016. The change in fair value of net trust assets, including REO was due to \$8.6 million in gains from changes in fair value of securitized mortgage borrowings, securitized mortgage collateral and investment securities available-for-sale primarily associated with a decrease in LIBOR as well as updated assumptions on certain later vintage trusts with improved performance. Partially offsetting the increase was a \$6.0 million decrease in NRV of REO during the period attributed to higher expected loss severities on properties held in the long-term mortgage portfolio during the period.

Income Taxes

We recorded income tax benefit of \$130 thousand and an expense of \$728 thousand for the three and nine months ended September 30, 2016 primarily the result of a return to provision adjustment for the 2015 tax return booked in the third quarter, amortization of the deferred charge, federal alternative minimum tax (AMT), and state income taxes from states where we do not have net operating loss carryforwards or state minimum taxes, including AMT. For the the three and nine months ended September 30, 2015, we recorded income tax expense (benefit) of

59

Table of Contents

\$781 thousand and (\$22.9) million, respectively. For the three months ended September 30, 2015, we recorded amortization of the deferred charge partially offset by a reduction in current income tax provision based upon an estimated reduction in federal AMT and state income taxes. For the nine months ended September 30, 2015, we recorded a benefit of \$24.4 million primarily the result of a reversal of valuation allowance partially offset by federal AMT, amortization of the deferred charge and state income taxes from states where we do not have net operating loss carryforwards or state minimum taxes, including AMT. The deferred charge represents the deferral of income tax expense on inter-company profits that resulted from the sale of mortgages from taxable subsidiaries to IMH prior to 2008. The deferred charge is amortized and/or impaired, which does not result in any tax liability to be paid. The deferred charge is included in other assets in the accompanying consolidated balance sheets and is amortized as a component of income tax expense in the accompanying consolidated statements of operations.

As of December 31, 2015, we had estimated federal and California net operating loss (NOL) carryforwards of approximately \$526.8 million and \$448.2 million, respectively. Federal and state NOL carryforwards begin to expire in 2027 and 2016, respectively.

Results of Operations by Business Segment

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

Mortgage Lending

	For the Three Months Ended September 30,			
	2016	2015	Increase (Decrease)	% Change
Gain on sale of loans, net	\$ 113,158	\$ 47,274	\$ 65,884	139 %
Servicing income, net	3,789	2,432	1,357	56
Loss on mortgage servicing rights	(15,857)	(4,818)	(11,039)	(229)
Other	18	(145)	163	112
Total revenues	101,108	44,743	56,365	126
Other income	1,092	658	434	66
Personnel expense	(37,996)	(20,631)	(17,365)	(84)
Business promotion	(10,310)	(10,702)	392	4
General, administrative and other	(5,578)	(4,494)	(1,084)	(24)
Accretion of contingent consideration	(1,591)	(2,424)	833	34
Change in fair value of contingent consideration	(23,215)	16,897	(40,112)	(237)
Net earnings before income taxes	\$ 23,510	\$ 24,047	\$ (537)	(2) %

For the three months ended September 30, 2016, gain on sale of loans, net were \$113.2 million compared to \$47.3 million in the comparable 2015 period. The \$65.9 million increase is primarily due to a \$49.3 increase in premiums from the sale of mortgage loans, a \$17.5 million increase in premiums from servicing retained loan sales and a \$8.5 million increase in realized and unrealized net gains on derivative financial instruments, partially offset by a \$7.2 million increase in direct loan origination expenses, a \$1.4 million decrease in MTM gains, and a \$907 thousand decrease in provision for repurchases.

The overall increase in gain on sale of loans, net was due to increased volumes and gain on sale margins. For the three months ended September 30, 2016, we originated and sold \$4.2 billion and \$4.1 billion of loans, respectively, as compared to \$2.3 billion and \$2.2 billion of loans originated and sold, respectively, during the same period in 2015. Margins increased to approximately 268 bps for the three months ended September 30, 2016 as compared to 205 bps for the same period in 2015 due to a higher concentration of retail loans which have higher margins.

For the three months ended September 30, 2016, servicing income, net was \$3.8 million compared to \$2.4 million in the comparable 2015 period. The increase in servicing income, net was the result of the servicing portfolio increasing 59% to an average balance of \$8.5 billion for the three months ended September 30, 2016 as compared to an average balance of \$5.4 billion for the three months ended September 30, 2015. The increase in the average balance of

Table of Contents

the servicing portfolio is a result of servicing retained loan sales of \$4.0 billion during the three months ended September 30, 2016

For the three months ended September 30, 2016, loss on MSR was \$15.9 million compared to \$4.8 million in the comparable 2015 period. For the three months ended September 30, 2016, we recorded an \$8.2 million loss from change in fair value of MSRs including \$9.4 million in MTM losses due to \$1.1 billion UPB of prepayments offset by a MTM gain at September 30, 2016 of \$1.2 million due to a slight increase in mortgage interest rates in September. As a result of our successful retention efforts, we recaptured and refinanced 85% of these prepayments at a lower coupon rate and thus a higher servicing value. Despite the MTM loss from loan prepayments recorded as a loss on MSRs, there was also a corresponding income from the recaptured loan with a higher MSR value recognized in gain on sale of loans, net in the consolidated statement of operations.

In addition to the MTM loss on MSRs, during the three months ended September 30, 2016 we had a \$7.5 million loss on sale of MSRs related to refunds of premiums to investors for loan payoffs associated with sales of servicing rights in previous periods as compared to \$471 thousand in the comparable 2015 period. During the third quarter of 2016, we amended a previous MSR sale agreement, extending the early prepayment protection, in return allowing the Company to solicit the sold portfolio. In the third quarter of 2016, the loss on mortgage servicing rights of \$7.5 million includes a \$2.8 million charge for third quarter 2016 activity and the remaining balance is primarily related to a reserve for potential future estimated premium recapture charges. As long as the interest rate environment allows for recapture opportunities, we expect to continue to refinance borrowers in the sold portfolio. However, we will monitor the profitability of this extended early prepayment protection on a month-to-month basis. The amendment gives the Company the option to terminate the agreement with a 90 day notification.

Personnel expense increased \$17.4 million to \$38.0 million for the three months ended September 30, 2016. The increase is primarily due to an increase in commission expense due to an increase in loan origination volumes as well as an increase in personnel related costs due to the addition of new sales personnel.

Business promotion was \$10.3 million for the three months ended September 30, 2016, compared to \$10.7 million for the comparable period of 2015. Our centralized call center purchases leads and promotes its business through radio and television advertisements. Despite the slight decrease in advertising expense, origination volume increased as we continue to focus on growing market share and geographic scope within the CashCall Mortgage retail channel, as well as continued growth in the correspondent and wholesale lending channels.

Beginning in the second quarter of 2015, as part of the acquisition of CCM, we record accretion of the contingent consideration liability from the close of the transaction in March 2015 through the end of the earn-out period in December 2017, which increases the contingent consideration liability. The estimated contingent consideration liability is based on discounted cash flows which represent the time value of money of the liability during the earn-out period. In the third quarter of 2016, accretion increased the contingent consideration liability by \$1.6 million as compared to \$2.4 million during the third quarter of 2015. The reduction in accretion is due to the reduction in the estimated future pre-tax earnings as compared to projections in 2015. The accretion will continue to be a charge against earnings in future quarters until the end of the earn-out period.

We recorded an \$23.2 million change in fair value associated with an increase in the contingent consideration liability for the third quarter of 2016 related to updated assumptions including current market conditions and increased mortgage loan originations for CCM. The change in fair value of contingent consideration was related to the estimated increase in future pre-tax earnings of CCM over the remaining earn-out period of five quarters. The fair value of contingent consideration may change from quarter to quarter based upon actual experience and updated assumptions used to forecast pre-tax earnings for CCM. Even though this projected increase in mortgage volume for CCM is favorable, it resulted in a corresponding charge to earnings of \$23.2 million in the third quarter of 2016.

Table of Contents

We recorded a \$2.9 million change in fair value associated with an increase in the contingent consideration liability for the first quarter of 2016 related to updated assumptions including current market conditions and increased mortgage loan originations for CCM. The change in fair value of contingent consideration was related to the estimated increase in future pre-tax earnings of CCM over the remaining earn-out period of seven quarters. The fair value of contingent consideration may change from quarter to quarter based upon actual experience and updated assumptions used to forecast pre-tax earnings for CCM. Beginning in the second quarter of 2015, as part of the acquisition of CCM, we record accretion of the contingent consideration liability from the close of the transaction in March 2015 through the end of the earn-out period in 2017, which increases the contingent consideration liability. The estimated contingent consideration liability is based on discounted cash flows which represent the time value of money of the liability during the earn-out period. In the first quarter of 2016, accretion increased the contingent consideration liability by \$1.9 million. We did not record accretion in the first quarter of 2015 as the acquisition transaction did not close until March 31, 2015, however the accretion will continue to be a charge against earnings in future quarters until the end of the earn-out period.

	For the Nine Months Ended September 30,			
	2016	2015	Increase (Decrease)	% Change
Gain on sale of loans, net	\$ 245,849	\$ 133,018	\$ 112,831	85 %
Servicing income, net	8,680	4,083	4,597	113
Loss on mortgage servicing rights	(41,249)	(14,176)	(27,073)	(191)
Other	70	(25)	95	380
Total revenues	213,350	122,900	90,450	74
Other income	2,148	1,673	475	28
Personnel expense	(92,334)	(55,252)	(37,082)	(67)
Business promotion	(30,721)	(19,496)	(11,225)	(58)
General, administrative and other	(15,214)	(11,351)	(3,863)	(34)
Accretion of contingent consideration	(5,244)	(5,471)	227	4
Change in fair value of contingent consideration	(34,569)	28,223	(62,792)	(222)
Net earnings before income taxes	\$ 37,416	\$ 61,226	\$ (23,810)	(39) %

Gain on sale of loans, net includes the operating expenses of CCM in the first quarter of 2015 before we closed the transaction on March 31, 2015. We received the economic benefit of the CCM transactions from the beginning of 2015 but did not hire the employees of CCM or incur direct operating expenditures of CCM until after the close of the transaction. Accordingly, operating expenses for CCM in the first quarter of 2015 were included within gain on sale

of loans, net as loan origination costs in the consolidated statements of operations. Beginning with the second quarter of 2015 the operating expenses of CCM were included in personnel, business promotion, general, administrative and other expense, as normally presented.

For the nine months ended September 30, 2016, gain on sale of loans, net were \$245.8 million compared to \$133.0 million in the comparable 2015 period. The \$112.8 million increase is primarily due to \$9.8 billion in originations for the nine months ended September 30, 2016 as compared to \$7.3 billion for the same period in 2015 as well as the presentation of CCM operating expenses in the first quarter of 2015.

For the nine months ended September 30, 2016, servicing income, net was \$8.7 million compared to \$4.1 million in the comparable 2015 period. The increase in servicing income, net was the result of the servicing portfolio increasing 78% to an average balance of \$6.4 billion for the nine months ended September 30, 2016 as compared to an average balance of \$3.6 billion for the nine months ended September 30, 2015. The increase in the average balance of the servicing portfolio is a result of servicing retained loan sales of \$9.1 billion during the nine months ended September 30, 2016 partially offset by a bulk sale of MSRs of approximately \$815.0 million.

For the nine months ended September 30, 2016, loss on MSRs was \$41.2 million compared to \$14.2 million in the comparable 2015 period. For the nine months ended September 30, 2016, we recorded a \$32.0 million loss from a change in fair value of MSRs primarily the result of \$2.4 billion in prepayments due to the low mortgage interest rate environment during the first nine months of 2016 which resulted in an increase in actual prepayments as well as prepayment speed assumptions. For the nine months ended September 30, 2016, as a result of our successful retention efforts, we recaptured and refinanced 83% of these prepayments at a lower coupon rate and thus a higher servicing value. Despite the MTM loss from loan prepayments recorded as a loss on MSRs, there was also a corresponding income from the recaptured loan with a higher MSR value recognized in gain on sale of loans, net in the consolidated statement of operations.

In addition to the MTM loss on MSRs, during the nine months ended September 30, 2016 we had a \$10.6 million loss on sale of mortgage servicing rights related to refunds of premiums to investors for loan payoffs associated with sales of servicing rights in previous periods as compared to \$6.2 million in the comparable 2015 period as well as a \$1.0 million loss on the sale of \$815.0 million UPB of MSRs. Partially offsetting the loss was a \$1.4 million increase in realized and unrealized gains from hedging instruments related to MSRs. During the third quarter of 2016, we amended a previous MSR sale agreement, extending the early prepayment protection, in return allowing the Company to solicit the sold portfolio. In the third quarter of 2016, the loss on mortgage servicing rights of \$7.5 million includes a \$2.8 million charge for third quarter 2016 activity and the remaining balance is primarily related to a reserve for potential future estimated premium recapture charges. As long as the interest rate environment allows for recapture opportunities, we expect to continue to refinance borrowers in the sold portfolio. However, we will monitor the profitability of this

Table of Contents

extended early prepayment protection on a month-to-month basis. The amendment gives the Company the option to terminate the agreement with a 90 day notification.

Beginning in the second quarter of 2015, as part of the acquisition of CCM, we record accretion of the contingent consideration liability from the close of the transaction in March 2015 through the end of the earn-out period in December 2017, which increases the contingent consideration liability. The estimated contingent consideration liability is based on discounted cash flows which represent the time value of money of the liability during the earn-out period. In the first nine months of 2016, accretion increased the contingent consideration liability by \$5.2 million. We did not record accretion in the first quarter of 2015 as the acquisition transaction did not close until March 31, 2015, however the accretion will continue to be a charge against earnings in the future five quarters until the end of the earn-out period.

We recorded a \$34.6 million change in fair value associated with an increase in the contingent consideration liability for the first nine months of 2016 related to updated assumptions including current market conditions and increased mortgage loan originations for CCM. The change in fair value of contingent consideration was related to the estimated increase in future pre-tax earnings of CCM over the remaining earn-out period of five quarters. The fair value of contingent consideration may change from quarter to quarter based upon actual experience and updated assumptions used to forecast pre-tax earnings for CCM. Even though this projected increase in mortgage volume for CCM is favorable, it resulted in a corresponding charge to earnings of \$34.6 million in the third quarter of 2016.

Real Estate Services

	For the Three Months Ended September 30,				
	2016	2015	Increase (Decrease)	% Change	
Real estate services fees, net	\$ 2,678	\$ 2,775	\$ (97)	(3)	%
Personnel expense	(1,863)	(1,156)	(707)	(61)	
General, administrative and other	(142)	(291)	149	51	
Net earnings before income taxes	\$ 673	\$ 1,328	\$ (655)	(49)	%

For the three months ended September 30, 2016, real estate services fees, net were \$2.7 million compared to \$2.8 million in the comparable 2015 period. The \$97 thousand decrease in real estate services fees, net was the result of a \$679 thousand decrease in real estate and recovery fees and a \$79 thousand decrease in real estate services partially offset by a \$661 thousand increase in loss mitigation fees. The decrease was primarily the result of a decrease in transactions related to the decline in the number of loans and the UPB of the long-term mortgage portfolio as compared to the third quarter of 2015.

	For the Nine Months Ended September 30,				
	2016	2015	Increase (Decrease)	% Change	
Real estate services fees, net	\$ 6,773	\$ 7,872	\$ (1,099)	(14)	%
Personnel expense	(4,721)	(3,787)	(934)	(25)	
General, administrative and other	(507)	(635)	128	20	
Net earnings before income taxes	\$ 1,545	\$ 3,450	\$ (1,905)	(55)	%

For the nine months ended September 30, 2016, real estate services fees, net were \$6.8 million compared to \$7.9 million in the comparable 2015 period. The \$1.1 million decrease in real estate services fees, net was the result of a \$1.5 million decrease in real estate and recovery fees and a \$14 thousand increase in real estate services partially offset by a \$411 thousand increase in loss mitigation fees. The decrease was primarily the result of a decrease in transactions related to the decline in the number of loans and the UPB of the long-term mortgage portfolio as compared to the first nine months of 2015.

Table of Contents

Long-Term Mortgage Portfolio

	For the Three Months Ended September 30,				
	2016	2015	Increase (Decrease)	% Change	
Other revenue	\$ 71	\$ 79	\$ (8)	(10)	%
Personnel expense	(3)	(155)	152	98	%
General, administrative and other	(99)	(108)	9	8	
Total expenses	(102)	(263)	161	61	
Net interest income	1,495	1,068	427	40	
Change in fair value of long-term debt	(8,641)	—	(8,641)	n/a	
Change in fair value of net trust assets, including trust REO gains (losses)	1,071	(3,004)	4,075	136	
Total other income (expense)	(6,075)	(1,936)	(4,139)	(214)	
Loss before income taxes	\$ (6,106)	\$ (2,120)	\$ (3,986)	(188)	%

For the three months ended September 30, 2016, net interest income totaled \$1.5 million as compared to \$1.1 million for the comparable 2015 period. Net interest income increased \$427 thousand for the quarter ended September 30, 2016 primarily attributable to a \$573 thousand increase in net interest spread on the long-term mortgage portfolio due to an improvement in net interest income and cash flows in trusts with residual interests. Partially offsetting the increase in interest income was a \$144 thousand increase in interest expense on the long-term debt due to an increase in 3 month LIBOR as compared to the prior year.

Change in the fair value of long-term debt resulted in an expense of \$8.6 million for the three months ended September 30, 2016, compared to no gain or loss for the comparable 2015 period as a result of an increase in the estimated fair value of long-term debt. The increase in the estimated fair value of long-term debt was primarily the result of a decrease in the discount rate attributable to an improvement in our own credit risk profile associated with our capital raise during the third quarter, improvement in our financial condition and results of operations from the mortgage lending segment during the third quarter of 2016.

The change in fair value related to our net trust assets (residual interests in securitizations) was a gain of \$1.1 million for the three months ended September 30, 2016, compared to a loss of \$3.0 million in the comparable 2015 period. The change in fair value of net trust assets, excluding REO was due to \$2.5 million in gains from changes in fair value of securitized mortgage borrowings, securitized mortgage collateral and investment securities available-for-sale primarily associated with a decrease in LIBOR as well as updated assumptions on certain later vintage trusts with improved performance. Additionally, the NRV of REO decreased \$1.4 million during the period attributed to higher expected loss severities on properties held in the long-term mortgage portfolio during the period.

Table of Contents

	For the Nine Months Ended September 30,				
	2016	2015	Increase (Decrease)	% Change	
Other revenue	\$ 183	\$ 203	\$ (20)	(10)	%
Personnel expense	(14)	(235)	221	94	%
General, administrative and other	(333)	(376)	43	11	
Total expenses	(347)	(611)	264	43	
Net interest income	4,259	3,458	801	23	
Change in fair value of long-term debt	(7,286)	(8,661)	1,375	16	
Change in fair value of net trust assets, including trust REO gains (losses)	2,609	(3,078)	5,687	185	
Total other income (expense)	(418)	(8,281)	7,863	95	
Loss before income taxes	\$ (582)	\$ (8,689)	\$ 8,107	93	%

For the nine months ended September 30, 2016, net interest income totaled \$4.3 million as compared to \$3.5 million for the comparable 2015 period. Net interest income increased \$801 thousand for the nine months ended September 30, 2016 primarily attributable to a \$1.1 million increase in net interest spread on the long-term mortgage portfolio due to an improvement in net interest income and cash flows in trusts with residual interests. Partially offsetting the increase in interest income was a \$261 thousand increase in interest expense on the long-term debt due to an increase in 3 month LIBOR as compared to the prior year.

Change in the fair value of long-term debt resulted in an expense of \$7.3 million for the nine months ended September 30, 2016, compared to an expense of \$8.7 million for the comparable 2015 period as a result of the increase in the estimated fair value of long-term debt. The increase in the estimated fair value of long-term debt during the nine months ended September 30, 2016 was primarily the result of a decrease in the discount rate attributable to an improvement in our own credit risk profile associated with our capital raise during the third quarter, improvement in our financial condition and results of operations from the mortgage lending segment during the third quarter of 2016. The increase in the estimated fair value of long-term debt during the 2015 was primarily the result of a decrease in the discount rate attributable to an improvement in our own credit risk profile, improvement in our financial condition and results of operations from the mortgage lending segment including the acquisition of CCM during the first quarter of 2015 as well as an increase in forward LIBOR interest rates during the second quarter of 2015.

The change in fair value related to our net trust assets (residual interests in securitizations) was a gain of \$2.6 million for the nine months ended September 30, 2016. The change in fair value of net trust assets, including REO was due to \$8.6 million in gains from changes in fair value of securitized mortgage borrowings, securitized mortgage collateral and investment securities available-for-sale primarily associated with a decrease in LIBOR as well as updated assumptions on certain later vintage trusts with improved performance. Partially offsetting the increase was a \$6.0 million decrease in NRV of REO during the period attributed to higher expected loss severities on properties held in the long-term mortgage portfolio during the period.

Table of Contents

Corporate

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

	For the Three Months Ended September 30,				
	2016	2015	Increase (Decrease)	% Change	
Interest expense	\$ (1,283)	\$ (1,607)	324	20	%
Other expenses	(426)	(1,558)	1,132	73	
Net loss before income taxes	\$ (1,709)	\$ (3,165)	\$ 1,456	46	%

For the three months ended September 30, 2016, interest expense decreased to \$1.3 million as compared to \$1.6 million for the comparable 2015 period. The \$324 thousand decrease in interest expense was primarily due to the conversion of the original \$20.0 million in Convertible Notes to common stock in January 2016. Additionally, in June 2016, we paid \$100 thousand extension fee to extend the maturity of the Term Financing to June 2017, which slightly increased interest expense as the fee is amortized using the effective yield method over the extended term of the financing.

For the September 30, 2016, other expenses decreased to \$426 thousand as compared to \$1.6 million for the comparable 2015 period. The decrease was primarily due to a \$806 thousand decrease in legal and professional fees as well as a \$768 thousand increase in allocated corporate expenses. The growth of the mortgage lending division resulted in increased allocations of certain corporate costs due to increased headcount. Partially offsetting the decrease was a \$432 thousand increase in data processing.

	For the Nine Months Ended September 30,				
	2016	2015	Increase (Decrease)	% Change	
Interest expense	\$ (4,371)	\$ (2,996)	(1,375)	(46)	%
Other expenses	(3,551)	(5,753)	2,202	38	
Net loss before income taxes	\$ (7,922)	\$ (8,749)	\$ 827	9	%

For the nine months ended September 30, 2016, interest expense increased to \$4.4 million as compared to \$3.0 million for the comparable 2015 period. The increase was primarily due to a \$1.5 million increase in interest expense from the \$30.0 million Term Financing issued in June of 2015 as well as a \$132 thousand increase attributable to the Convertible Notes. The increase in interest expense on the Convertible Notes is primarily related to the timing of the transaction as it was entered into in May 2015 as well as \$129 thousand of debt issuance costs accelerated upon conversion of the 2013 Notes in January 2016. Partially offsetting the increase in interest expense was a \$399 thousand decrease in interest expense related to the payoff of the short-term borrowings in 2015.

For the nine months ended September 30, 2016, other expenses decreased to \$3.6 million as compared to \$5.8 million for the comparable 2015 period. The decrease was primarily due to an \$1.7 million increase in allocated corporate

expenses, a \$617 thousand decrease in occupancy expense as well as a \$511 thousand decrease in legal and professional fees. The growth of the mortgage lending division resulted in increased allocations of certain corporate costs due to increased headcount. Partially offsetting the decrease was a \$711 thousand increase in data processing.

ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to a variety of operational and market risks. Refer to the complete discussion of operational and market risks included in Part II, Item 7 of our report on Form 10-K for the year ended December 31, 2015. There has been no material change to the types of market and operational risks faced by us.

Table of Contents

Interest Rate Risk

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

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

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

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

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

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

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

Table of Contents

Sensitivity Analysis

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

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

We used September 30, 2016 market rates on our instruments to perform the sensitivity analysis. The estimates are based on the market risk sensitivity and assume instantaneous, parallel shifts in interest rate yield curves. Management uses sensitivity analysis, such as those summarized below, based on a hypothetical 25 basis point increase or decrease in interest rates, to monitor the risks associated with changes in interest rates. We believe the use of a 50 basis point shift up and down (100 basis point range) is appropriate given the relatively short time period that the mortgage loans pipeline is held on our balance sheet and exposed to interest rate risk (during the processing, underwriting and closing stages of the mortgage loans which can last up to approximately 60 days). We also actively manage our risk management strategy for our mortgage loans pipeline (through the use of economic hedges such as forward loan sale commitments and mandatory delivery commitments) and generally adjust our hedging position daily. In analyzing the interest rate risks associated with our MSR's, management also uses multiple sensitivity analyses (hypothetical 25 and 50 basis point increases and decreases) to review the interest rate risk associated with our MSR's.

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

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

The following table summarizes the estimated changes in the fair value of our mortgage pipeline, MSR's and related derivatives that are sensitive to interest rates as of September 30, 2016 given hypothetical instantaneous parallel shifts in the yield curve:

	Changes in Fair Value			
	Down 50 bps	Down 25 bps	Up 25 bps	Up 50 bps
Total mortgage pipeline (1)	(2)	(74)	(58)	(367)
Mortgage servicing rights (2)	(13,517)	(6,825)	6,624	12,929

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

ITEM 4: CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

The Company maintains disclosure controls and procedures (as defined in the Securities Exchange Act of 1934 Rules 13a-15(e) or 15d-15(e)) designed to ensure that information required to be disclosed in reports filed or submitted

68

Table of Contents

under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by the Company in its reports that it files or submits under the Exchange Act is accumulated and communicated to the Company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

As required by Rules 13a-15 and 15d-15 under the Exchange Act, in connection with the filing of this Quarterly Report on Form 10-Q, our management, under the supervision and with the participation of our CEO and CFO, conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rule 13a-15(e). Based on that evaluation, the Company's chief executive officer and chief financial officer concluded that, as September 30, 2016, the Company's disclosure controls and procedures were effective at a reasonable assurance level.

Changes in Internal Control Over Financial Reporting

There has been no change in the Company's internal control over financial reporting during the Company's quarter ended September 30, 2016, that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Table of Contents

PART II. OTHER INFORMATION

ITEM 1: LEGAL PROCEEDINGS

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

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

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

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

Please refer to IMH's report on Form 10-K for the year ended December 31, 2015 for a description of litigation and claims.

ITEM 1A: RISK FACTORS

None.

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

None.

ITEM 3: DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4: MINE SAFETY DISCLOSURES

None.

ITEM 5: OTHER INFORMATION

None.

70

Table of Contents

ITEM 6: EXHIBITS

- (a) Exhibits:
- 10.1 2010 Omnibus Incentive Plan, as amended (incorporated by reference to Exhibit 10.1 of the Company's Current Report Form 8-K filed with the Securities and Exchange Commission on July 21, 2016).
 - 10.2 Amendment to employment agreement dated September 8, 2016 between Impac Mortgage Holdings, Inc. and Ron Morrison (incorporated by reference to Exhibit 10.1 of the Company's Current Report Form 8-K filed with the Securities and Exchange Commission on September 8, 2016).
 - 10.3 Amendment to employment agreement dated September 8, 2016 between Impac Mortgage Holdings, Inc. and Todd Taylor (incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on September 8, 2016).
 - 31.1 Certification of Chief Executive Officer pursuant to Item 601(b)(31) of Regulation S-K, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
 - 31.2 Certification of Chief Financial Officer pursuant to Item 601(b)(31) of Regulation S-K, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
 - 32.1* Certifications of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
 - 101 The following materials from Impac Mortgage Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended September 30, 2016, formatted in XBRL (Extensible Business Reporting Language): (1) the Condensed Consolidated Balance Sheets, (2) the Condensed Consolidated Statements of Operations, (3) the Condensed Consolidated Statements of Cash Flows, and (4) Notes to Consolidated Financial Statements, tagged as blocks of text.

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

Table of Contents

SIGNATURES

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

IMPAC MORTGAGE HOLDINGS, INC.

/s/ TODD R. TAYLOR

Todd R. Taylor

Chief Financial Officer

(authorized officer of registrant and principal financial officer)

November 7, 2016