

NB CAPITAL CORP  
Form 10-Q  
August 14, 2003

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

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended June 30, 2003

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file Number: 1-14103

**NB CAPITAL CORPORATION**

(Exact name of registrant as specified in its charter)

**Maryland**  
(Jurisdiction of incorporation)

**52-2063921**  
(I.R.S. Employer Identification No.)

**125 West 55th Street,  
New York, New York**  
(Address of principal executive offices)

**10019**  
(Zip Code)

**212-632-8580**

(Registrant's telephone number, including area code)

**(N/A)**

(Former name, former address and former fiscal year, if changed since last report)

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 is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes  No

**Applicable only to issuers involved in bankruptcy proceedings during the preceding five years:**

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Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13, or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by the court.

Yes \_\_\_\_\_ No \_\_\_\_\_

## Applicable only to corporate issuers:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at August 14, 2003
Common Stock par value \$0.01 per share	100

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## NB CAPITAL CORPORATION

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This report contains certain forward-looking statements and information relating to NB Capital Corporation (the Company or NB Capital) that are based on the beliefs of the Company's management as well as assumptions made by and information currently available to the Company.

Applicable only to corporate issuers:

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management. When used in this report, the words anticipate, believe, estimate, expect and similar expressions, as they relate to the Company or the Company's management, are intended to identify forward-looking statements. Such statements reflect the current view of the Company's management with respect to future events and the Company's future performance and are subject to certain risks, uncertainties and assumptions. Should management's current view of the future or underlying assumptions prove incorrect, actual results may vary materially from those described herein as anticipated, believed, estimated or expected. The Company does not intend to update these forward-looking statements.

References to \$ are to United States dollars; references to C\$ are to Canadian dollars. As of June 30, 2003, the Canadian dollar exchange rate was C\$1.3475 = \$1.00 and certain amounts stated herein reflect such exchange rate.

### ***NB CAPITAL CORPORATION***

#### ***BALANCE SHEETS***

<i>(in thousands of US dollars)</i>	<b>June 30, 2003 Unaudited</b>	<b>December 31 2002</b>
<b>Assets</b>		
	\$	\$
Cash and cash equivalents	25,585	5,454
Due from an affiliated company	16,937	6,977
Promissory notes	445,660	469,847
Accrued interest on cash equivalents	3	-
	<b>488,185</b>	<b>482,278</b>
<b>Liabilities</b>		
Due to the parent company	390	345
Accounts payable	22	41
	412	386
<b>Stockholders' equity</b>		
Capital stock and Additional paid-in capital (see detail note 6)	476,764	476,764
Retained earnings	11,009	5,128
	487,773	481,892
	<b>488,185</b>	<b>482,278</b>

See accompanying notes to financial statements.

**NB CAPITAL CORPORATION****STATEMENTS OF INCOME***(Unaudited)*

<i>(in thousand of US dollars)</i>	Three-month periods ended		Six-month periods ended	
	2003	June 30, 2002	2003	June 30, 2002
<b>Revenue</b>				
Interest income	\$	\$	\$	\$
Cash equivalents	116	140	170	249
Promissory notes	9,556	9,121	19,132	18,609
	<b>9,672</b>	<b>9,261</b>	<b>19,302</b>	<b>18,858</b>
<b>Expenses</b>				
Servicing and advisory fees	390	347	758	695
Legal and other professional fees	64	45	129	115
	<b>454</b>	<b>392</b>	<b>887</b>	<b>810</b>
<b>Net income</b>	<b>9,218</b>	<b>8,869</b>	<b>18,415</b>	<b>18,048</b>
Preferred stock dividends	6,267	6,268	12,534	12,535
<b>Income available to common stockholders</b>	<b>2,951</b>	<b>2,601</b>	<b>5,881</b>	<b>5,513</b>
Weighted-average number of common shares outstanding	100	100	100	100
<b>Earnings per common share - basic and diluted</b>	<b>30</b>	<b>26</b>	<b>59</b>	<b>55</b>

See accompanying notes to financial statements

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**NB CAPITAL CORPORATION****STATEMENTS OF STOCKHOLDERS' EQUITY**

Applicable only to corporate issuers:

*(Unaudited)*

<i>(in thousand of US dollars)</i>	Three-month periods ended		Six-month periods ended	
	June 30,		June 30,	
	2003	2002	2003	2002
<b>PREFERRED STOCK</b>	\$	\$	\$	\$
Balance, beginning and end of period	3	3	3	3
<b>COMMON STOCK AND PAID-IN CAPITAL</b>				
Balance, beginning and end of period	476,761	476,761	476,761	476,761
<b>RETAINED EARNINGS</b>				
Balance, beginning of period	8,058	7,555	5,128	4,643
Net income	9,218	8,869	18,415	18,048
Preferred stock dividends	(6,267)	(6,268)	(12,534)	(12,535)
Balance, end of period	<b>11,009</b>	<b>10,156</b>	<b>11,009</b>	<b>10,156</b>
<b>TOTAL STOCKHOLDERS' EQUITY</b>	<b>487,773</b>	<b>486,920</b>	<b>487,773</b>	<b>486,920</b>

See accompanying notes to financial statements.

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***NB CAPITAL CORPORATION******STATEMENTS OF CASH FLOWS****Unaudited*

<i>(in thousands of US dollars)</i>	Six-month periods ended	
	June 30,	
	2003	2002
<b>OPERATING ACTIVITIES</b>	\$	\$

Applicable only to corporate issuers:

*Unaudited*

	<b>Six-month periods ended June 30,</b>	
Net income	18,415	18,048
Items not affecting cash resources		
Due from an affiliated company	(9,960)	3,871
Due to the parent company	45	16
Accounts payable	(19)	(14)
Accrued interest receivable on cash equivalents	(3)	6
<b>Net cash provided by operating activities</b>	<b>8,478</b>	<b>21,927</b>
<b>FINANCING ACTIVITIES</b>		
Dividends	(12,534)	(12,535)
<b>Net cash used in financing activities</b>	<b>(12,534)</b>	<b>(12,535)</b>
<b>INVESTING ACTIVITIES</b>		
Investment in promissory notes	(70,420)	(136,087)
Repayments of promissory notes	94,607	82,942
<b>Net cash used in investing activities</b>	<b>24,187</b>	<b>(53,145)</b>
Cash and cash equivalents, beginning of period	5,454	53,765
<b>Cash and cash equivalents, end of period</b>	<b>25,585</b>	<b>10,012</b>

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See accompanying notes to financial statements.

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## ***NB CAPITAL CORPORATION***

### ***NOTES TO THE FINANCIAL STATEMENTS***

*June 30, 2003*

(unaudited)

*(in thousand of U.S. dollars)*

#### **1) Incorporation and nature of operations**

Applicable only to corporate issuers:

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NB Capital Corporation (the Company) was incorporated in the State of Maryland on August 20, 1997. The Company's principal business is to acquire, hold, finance and manage mortgage assets. The Company issued, through an Offering Circular dated August 22, 1997, \$300,000 of preferred stock and simultaneously, National Bank of Canada, the Company's parent company, made a capital contribution in the amount of \$183,000. The Company used the aggregate net proceeds of \$477,000 to acquire promissory notes (Promissory notes) issued by NB Finance, Ltd., a wholly-owned subsidiary of National Bank of Canada.

### 2) Significant accounting policies

#### *Financial statements*

The financial statements are prepared in accordance with accounting principles generally accepted in the United States of America and are expressed in U.S. dollars.

The interim financial statements for the three-month and six-month periods are unaudited, however, the financial statements include, in the opinion of management, all adjustments necessary for a fair presentation. The unaudited financial statements should be read in conjunction with the audited financial statements included in the Company's annual report filed on Form 10-K. The results of the interim financial statements may not be an indicator of the results anticipated in the full year.

#### *Promissory notes*

In accordance with Statements of Financial Accounting Standards (SFAS) No.115 Accounting for certain Investments in debt and equity Securities and based on the Company's intentions regarding these instruments, the Company has classified the Promissory notes as held to maturity and has accounted for them at amortized cost.

#### *Income taxes*

The Company has elected to be taxed as a Real Estate Investment Trust (REIT) under the *Internal Revenue Code of 1986*, as amended, and accordingly, is generally not liable for United States federal income tax to the extent that it distributes at least 90% of its taxable income to its stockholders, maintains its qualification as a REIT and complies with certain other requirements.

#### *Per share data*

Basic and diluted earnings per share with respect to the Company for the three-month and six-month periods ended June 30, 2003 and 2002 are computed based upon the weighted average number of common shares outstanding during the period.

#### *Estimates*

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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. Actual results could differ from those estimates.

**NOTES TO THE FINANCIAL STATEMENTS**

June 30, 2003

(unaudited)

(in thousand of U.S. dollars)

**3) Promissory notes**

The Company entered into loan agreements evidenced by Promissory notes with NB Finance, Ltd., an affiliated company. The Promissory notes are collateralized by mortgage loans which are secured by residential first mortgages and insured by the Canada Mortgage and Housing Corporation.

The promissory notes have maturities ranging from July 2003 to December 2012, at rates ranging from 7.31% to 10.21%, with a weighted average rate of approximately 8.61% per annum.

These rates approximate market interest rates for loans of similar credit and maturity provisions and, accordingly, management believes that the carrying value of the promissory notes receivable approximates their fair value.

Promissory notes as of March 31, 2003	\$ 436,225
Acquisitions	70,420
Principal repayments	(60,985)
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Promissory notes as of June 30, 2003	\$ 445,660
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The scheduled principal repayments as of June 30, 2003 are as follows:

2003	\$34,650	2009	29,877
2004	101,402	2010	37,043
2005	80,953	2011	14,890
2006	73,375	2012	36,320
2007	11,375		
2008	25,775		

**4) Transactions with an affiliated company**

During the three-month and six-month periods ended June 30, 2003 and June 30, 2002, the Company earned interest from NB Finance, Ltd. on the Promissory notes in the amount of \$9,556 (\$9,121 in 2002) and \$19,132 (\$18,609 in 2002) respectively (see Note 3).

The amount of \$16,937 due from an affiliated company as of June 30, 2003 and \$6,977 as of December 31, 2002 represent interest and principal repayments due on the promissory notes.

**5) Transactions with the parent company**

The Company entered into agreements with National Bank of Canada in relation to the administration of the Company's operations. The agreements are as follows:

**Advisory agreement**

In exchange for a fee equal to \$30 per year, payable in equal quarterly installments, National Bank of Canada will furnish advice and recommendations with respect to all aspects of the business and affairs of the Company. During the three-month periods ended June 30, 2003 and June 30, 2002, fees of \$7 were charged to the Company.



**NB CAPITAL CORPORATION****NOTES TO THE FINANCIAL STATEMENTS***June 30, 2003*

(unaudited)

*(in thousand of U.S. dollars)***5) Transactions with the parent company (continued)*****Servicing agreement***

National Bank of Canada services and administers the Promissory notes and the collateralized mortgage loans and performs all necessary operations in connection with such servicing and administration.

The fee equals to one-twelfth (1/12) of 0.25% per annum of the aggregate outstanding balance of the collateralized mortgage loans as of the last day of each calendar month. For the three-month periods ended June 30, 2003 and June 30, 2002, the average outstanding balance of the collateralized mortgage loans were \$557,115 and \$547,208 respectively. During the three-month periods ended June 30, 2003 and June 30, 2002, fees of \$383 and \$340 respectively, were charged to the Company.

***Custodial agreement***

National Bank of Canada holds all documents relating to the collateralized mortgage loans. During the three-month periods ended June 30, 2003 and June 30, 2002, no fee was charged to the Company.

**6) Stockholders equity***(in U.S. Dollars)****Common stock***

The Company is authorized to issue up to 1,000 shares of \$ 0.01 par value common stock.

***Preferred stock***

The Company is authorized to issue up to 10,000,000 shares of \$0.01 par value preferred stock as follows:

300,000 shares have been authorized and issued as 8.35% Non-cumulative Exchangeable Preferred Stock, Series A, non-voting, ranked senior to the common stock and junior to the Adjustable Rate Cumulative Senior Preferred Shares, with a liquidation value of \$1,000 per share, redeemable at the Company's option on or after September 3, 2007, except upon the occurrence of certain changes in tax laws in the United States of America and in Canada, on or after September 3, 2002. These Series A shares are traded on the New York Stock Exchange in the form of Depositary Shares, each representing a one-fortieth interest therein.

Each Series A share is exchangeable, upon the occurrence of certain events, for one newly issue 8.45% Non-cumulative First Preferred Share, Series Z, of National Bank of Canada.

1,000 shares authorized and 110 shares issued as Adjustable Rate Cumulative Senior Preferred Shares, non-voting, ranked senior to the common stock and to the 8.35% Non-cumulative Exchangeable Preferred Stock, Series A, with a liquidation value of

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\$3,000 per share, redeemable at the Company's option at any time and retractable at the holder's option on December 30, 2007 and every ten-year anniversary thereof.

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

The Company's principal business objective is to acquire, hold, finance and manage assets consisting of obligations secured by real property as well as other qualifying REIT assets ( Mortgage Assets ). The Company has elected to be taxed as a REIT under the Internal Revenue Code of 1986, as amended and, accordingly, is generally not liable for United States federal income tax to the extent that it distributes at least 90% of its taxable income, subject to certain adjustments, to its stockholders.

#### **Critical accounting policies**

We believe that there are no critical accounting policies in connection with the preparation of the financial statements of NB Capital Corporation.

#### **Results of operations:**

*(in thousands of U.S. dollars)*

For the three-month periods ended June 30, 2003 and June 30, 2002, the Company reported net income of \$9,218 and \$8,869 respectively. Revenues, which were comprised entirely of interest income, were \$9,672 and \$9,261 respectively, and expenses were \$454 and \$392, respectively. Since the Company has elected to be taxed as a REIT, no income tax was recorded during the period.

Ninety-nine percent of revenues for the three-month period ended June 30, 2003 and the ninety-eight percent of revenues for the three-month period ended June 30, 2002 were derived from the Mortgage Assets issued by NB Finance, Ltd., an affiliated company ( NB Finance ). The Mortgage Assets issued by NB Finance are collateralized by the Mortgage Loans that consist of fifty-eight pools of residential first mortgages insured by Canada Mortgage and Housing Corporation and which are secured by real property located in Canada. The balance of the revenues result from interest on cash equivalents.

Expenses for the three-month periods ended June 30, 2003 and 2002 totaled \$454 and \$392, respectively, of which \$390 and \$347, respectively, represent servicing and advisory fees paid to National Bank of Canada, the Company's direct parent (the Bank ) pursuant to the Servicing Agreement between the Bank and the Company (the Servicing Agreement ) and the Advisory Agreement between the Bank and the Company (the Advisory Agreement ), whereby the Bank performs all necessary operations in connection with administering the Mortgage Assets issued by NB Finance and the Mortgage Loans. Legal and other professional fees include payment to the transfer agent and other professional fees.

During the three-month period ended June 30, 2003, the Board of Directors of the Company authorized dividends, in the aggregate, of \$6,267 compared to \$6,268 for the three-month period ended June 30, 2002, on its Preferred Stock (i.e., Adjustable Rate Cumulative Senior Preferred Shares (the Senior Preferred Shares ) and 8.35% Non-cumulative Exchangeable Preferred Stock, Series A (the Series A Preferred Shares ) and, accordingly, the Depository Shares). Such dividends were paid on June 30, 2003.

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

(continued)

#### **Capital Resources and Liquidity:**

*(in thousands of U.S. dollars)*

The Company's revenues are derived from the Mortgage Assets. As of June 30, 2003, \$446 million of Mortgage Assets issued by NB Finance were over-collateralized by the C\$841 million (\$624 million) of Mortgage Loans. The Company believes that the amounts generated from the

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payment of interest and principal on such Mortgage Loans will provide more than sufficient funds to make full payments with respect to the Mortgage Assets issued by NB Finance and that such payments will provide the Company with sufficient funds to meet its operating expenses and to pay quarterly dividends on the Senior Preferred Shares and the Series A Preferred Shares and, accordingly, the Depositary Shares. To the extent that the cash flow from its Mortgage Assets exceeds those amounts, the Company will use the excess to fund the acquisition of additional Mortgage Assets and make distributions on the Common Stock.

The Company does not require any capital resources for its operations and, therefore, it is not expected to acquire any capital assets in the foreseeable future.

As of June 30, 2003, the Company had cash equivalents of \$25,585 representing 5.24% of total assets, compared to \$5,454 representing 1.1% of total assets, as of December 31, 2002. The increase in liquidity is attributable to repayment of Mortgage Assets. It is expected that the Company will invest in additional Mortgage Assets once cash resources close by without exceeding 20% of total assets. While this continues to be the Company's investment policy, the Company maintains flexibility in this regard. On May 27, 2003, the Company bought \$70 million in additional Mortgage Assets in order to reduce increased liquidity. The liquidity level is sufficient for the Company to pay fees and expenses pursuant to the Servicing Agreement and the Advisory Agreement.

The Company's principal short-term and long-term liquidity needs are to pay quarterly dividends on the Senior Preferred Shares and the Series A Preferred Shares and, accordingly, the Depositary Shares, to pay fees and expenses of the Bank pursuant to the Servicing Agreement and the Advisory Agreement, and to pay franchise fees and expenses of advisors, if any.

The Company does not have any indebtedness (current or long-term), other material capital expenditures, balloon payments or other payments due on other long-term obligations. No negative covenants have been imposed on the Company.

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### **Disclosure About Market Risk**

Any market risk to which the Company would be exposed would result from fluctuations in (a) interest rates and (b) currency exchange rates affecting the interest payments received by the Company in respect of the Mortgage Assets issued by NB Finance. Since the Mortgage Assets are significantly overcollateralized by the Mortgage Loans, interest rate fluctuations should not present significant market risk. The Company expects that the interest and principal generated by the Mortgage Loans should enable full payment by NB Finance of all of its obligations as they became due. Since the Mortgage Loans are guaranteed by a fixed ratio of exchange, predetermined on the date of purchase and applicable until the maturity of the Mortgage Loans pursuant to the Mortgage Loan Assignment Agreement, fluctuations in currency exchange rates should not present significant market risk.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

This information is included under Item 2 of this report under the caption "Disclosure About Market Risk".

### **ITEM 4. CONTROLS AND PROCEDURES**

Based on their evaluation as of the end of the period covered by this report, the Company's President and Chief Financial Officer have concluded that the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act of 1934, as amended (the Exchange Act)) are effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission rules and forms.

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## **PART II. OTHER INFORMATION**

### **ITEM 1. LEGAL PROCEEDINGS**

The Company is not involved in any pending legal proceedings other than routine legal proceedings occurring in the ordinary course of business, which involve amounts in the aggregate believed by management to be immaterial to the financial condition of the Company.

ITEM 2. CHANGES IN SECURITIES

Not applicable.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

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

Not applicable.

ITEM 5. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits:

Exhibit	Description
11	Computation of Earnings Per Share
31.1	Certification of Chairman and President pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Written Statement of Chairman and President Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350)
32.2	Written Statement of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350)

(b) Reports on Form 8-K:

No Reports on Form 8-K were filed during the quarter for which this report is filed.

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**SIGNATURES**

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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.

NB CAPITAL CORPORATION

Date August 14, 2003

/s/ Serge Lacroix  
Serge Lacroix  
Director

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