IRWIN FINANCIAL CORP
Form 10-K
March 09, 2005

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-K

(Mark One)

þ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 19341933

For the fiscal Year Ended December 31, 2004

or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 19341934

For the transition period from to .

Commission file number 0-6835

IRWIN FINANCIAL CORPORATION

(Exact name of Corporation as Specified in its Charter)

Indiana **(State or Other Jurisdiction of Incorporation or Organization)**	**35-1286807** **(I.R.S. Employer Identification No.)**
500 Washington Street Columbus, Indiana **(Address of Principal Executive Offices)**	**47201** **(Zip Code)**
(812) 376-1909 **(Corporation s Telephone Number, Including Area Code)**	**www.irwinfinancial.com** **(Web Site)**

Securities registered pursuant to Section 12(b) of the Act: None

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

Title of Class:	**Common Stock***
Title of Class:	**10.50% Cumulative Trust Preferred Securities issued by IFC Capital Trust II and the guarantee with respect thereto.**
Title of Class:	**8.75% Cumulative Convertible Trust Preferred Securities issued by IFC Capital Trust III and the guarantee with respect thereto.**
Title of Class	**8.70% Cumulative Trust Preferred Securities issued by IFC Capital Trust VI and the guarantee with respect thereto.**

Indicate by check mark whether the Corporation: (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 Corporation was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

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

Indicate by check mark whether the Corporation is an accelerated filer (as defined in Exchange Act Rule 12b-2). Yes þ No o

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant, based on the closing price for the registrant s common stock on the New York Stock Exchange on June 30, 2004, was approximately $460,798,377.

The aggregate market value of the voting stock held by non-affiliates of the Corporation was $425,686,165 as of February 18, 2005. As of February 18, 2005, there were outstanding 28,506,964 common shares of the Corporation.

* Includes associated rights.

Documents Incorporated by Reference

Selected Portions of the Following Documents	Part of Form 10-K Into Which Incorporated
Definitive Proxy Statement for Annual Meeting Shareholders to be held April 7, 2005 **Exhibit Index on Pages 121 through 123**	**Part III**

FORM 10-K

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Redemption and Loan Repayment Agreement
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Tax Gross-Up Agreement
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Code of Conduct
Subsidiaries

Consent of Registered Public Accounting Firm
Certification by the CEO
Certification by the CFO
Certification of the CEO
Certification of the CFO

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PART I

Item 1. *Business*
General

We are a diversified financial services company headquartered in Columbus, Indiana with $524.9 million of net revenues in 2004 and $5.2 billion in assets at December 31, 2004. We focus primarily on the extension of credit to consumers and small businesses as well as providing the ongoing servicing of those customer accounts. Through our direct and indirect subsidiaries, we currently operate five major lines of business: mortgage banking, commercial banking, home equity lending, commercial finance and venture capital. More recently, our venture capital business has assumed a lesser role in our consolidated results.

We are a regulated bank holding company and we conduct our consumer and commercial lending businesses through various operating subsidiaries. Our banking subsidiary, Irwin Union Bank and Trust Company, was organized in 1871. We formed the holding company in 1972. Our direct and indirect major subsidiaries include Irwin Union Bank and Trust Company, a commercial bank, which together with Irwin Union Bank, F.S.B., a federal savings bank, conduct our commercial banking activities; Irwin Mortgage Corporation, a mortgage banking company; Irwin Home Equity Corporation, a consumer home equity lending company; Irwin Commercial Finance Corporation, a commercial finance subsidiary; and Irwin Ventures LLC, a venture capital company.

At the parent level, we work actively to add value to our lines of business by interacting with the management teams, capitalizing on interrelationships, providing centralized services and coordinating overall organizational decisions. Additionally, as discussed in more detail later in this report on Risk Management the parent company also provides risk management oversight and controls for our subsidiaries. Under this organizational structure, the majority of our mortgage banking, home equity lending and commercial finance lines of business operate as direct and indirect subsidiaries of Irwin Union Bank and Trust. This structure provides additional liquidity and results in regulatory oversight of our business.

Our Internet address is *http://www.irwinfinancial.com.*

We make available free of charge through our Internet website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports as soon as reasonably practicable after we electronically file the material with the Securities and Exchange Commission (SEC). Our Internet website and the information contained or incorporated in it are not intended to be incorporated into this Annual Report on Form 10-K.

Major Lines of Business

Mortgage Banking

We established our mortgage banking line of business when we acquired our subsidiary, Irwin Mortgage Corporation, formerly Inland Mortgage Corporation, in 1981. Irwin Mortgage became a subsidiary of Irwin Union Bank and Trust in October, 2002. In this line of business, Irwin Mortgage originates, purchases, sells, and services primarily conventional and government agency-backed residential mortgage loans throughout the United States. Most of our first mortgage originations either are insured or guaranteed by an agency of the federal government, such as the Federal Housing Authority (FHA) or the Veterans Administration (VA) or, in the case of conventional mortgages, meet requirements for resale to the Federal National Mortgage Association (FNMA), the Federal Home Loan Mortgage Corporation (FHLMC) or the Federal Home Loan Bank (FHLB). We originate mortgage loans through retail offices and through direct marketing. We also purchase mortgage loans through mortgage brokers and loan correspondents. Our relationships with realtors, homebuilders, brokers and correspondents help us identify potential borrowers. Irwin Mortgage also engages in the mortgage reinsurance business through its subsidiary, Irwin Reinsurance Corporation, a Vermont corporation. We sell mortgage loans to institutional and private investors but may retain servicing rights to the loans we originate or purchase. Irwin Mortgage collects and accounts for the monthly payments

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on each loan serviced and pays the real estate taxes and insurance necessary to protect the integrity of the mortgage lien, for which it receives a servicing fee.

At January 31, 2005, Irwin Mortgage operated 169 production and satellite offices in 33 states. We discuss this line of business further in the Mortgage Banking section of Management s Discussion and Analysis of Financial Condition and Results of Operations (MD&A) of this report.

Commercial Banking

Our commercial banking line of business provides credit, cash management and personal banking products primarily to small businesses and business owners. We offer commercial banking services through our banking subsidiaries, Irwin Union Bank and Trust Company, an Indiana state-chartered commercial bank, and Irwin Union Bank, F.S.B., a federal savings bank. The commercial banking line of business offers a full line of consumer, mortgage and commercial loans, as well as personal and commercial checking accounts, savings and time deposit accounts, personal and business loans, credit card services, money transfer services, financial counseling, property, casualty, life and health insurance agency services, trust services, securities brokerage and safe deposit facilities. This line of business operates through two charters:

Irwin Union Bank and Trust Company headquartered in Columbus, Indiana and organized in 1871, is a full service Indiana state-chartered commercial bank with offices currently located throughout nine counties in central and southern Indiana, as well as in Kalamazoo, Grandville (near Grand Rapids), Traverse City and Lansing, Michigan; Carson City and Las Vegas, Nevada; and Salt Lake City, Utah.

Irwin Union Bank, F.S.B. headquartered in Louisville, Kentucky, is a full-service federal savings bank that began operations in December 2000. Currently we have offices located in Clayton, Missouri (near St. Louis); Louisville, Kentucky; Milwaukee Wisconsin; Phoenix, Arizona; and, Sacramento, California.

In 2004, our Las Vegas and Salt Lake City branches of Irwin Union Bank, F.S.B. were sold to Irwin Union Bank and Trust Company.

We discuss this line of business further in the Commercial Banking section of the MD&A of this report.

Home Equity Lending

We established this line of business when we formed Irwin Home Equity Corporation as our subsidiary in 1994. It is headquartered in San Ramon, California. Irwin Home Equity became a subsidiary of Irwin Union Bank and Trust in 2001. In conjunction with Irwin Union Bank and Trust, Irwin Home Equity originates, purchases, securitizes and services home equity loans and lines of credit and first mortgages nationwide. Our target customers are principally credit worthy, home owning consumers who are active, unsecured credit card debt users. We market our home equity products (with loan-to-value ratios up to 125%) and first mortgage refinance programs (with loan-to-value ratios up to 100%) through direct mail, the Internet, mortgage brokers and correspondent lenders nationwide. Irwin Home Equity s core competencies are credit risk assessment and specialized home loan servicing.

We established Irwin Residual Holdings Corporation and Irwin Residual Holdings Corporation II in 2001 to hold residual interests that Irwin Union Bank and Trust Company transferred to Irwin Financial Corporation. The residual interests were created as a result of securitizations in our home equity line of business.

We discuss this line of business further in the Home Equity Lending section of the MD&A of this report.

Commercial Finance

Established in 1999, our commercial finance line of business originates small-ticket equipment leases through an established North American network of vendors and third-party originators and provides financing

for franchisees of qualified quick service and casual dining restaurant concepts in the United States. The majority of our leases are full payout (no residual), small-ticket assets secured by commercial equipment. We finance a variety of commercial and office equipment types and try to limit the industry and geographic concentrations in our lease and loan portfolios. Loans to franchisees may include the financing of real estate as well as equipment.

In July 2000, the commercial finance line of business acquired an ownership of approximately 78% in Irwin Commercial Finance Canada Corporation (ICFCC), formerly Onset Capital Corporation, a Canadian small-ticket equipment leasing company headquartered in Vancouver, British Columbia. In December 2001, Onset Capital established Onset Alberta Ltd. as a subsidiary to facilitate its leasing business. In October 2001, we formed Irwin Franchise Capital Corporation to conduct our franchise lending business. We established Irwin Commercial Finance Corporation (formerly, Irwin Capital Holdings) in April 2001 as a subsidiary of Irwin Union Bank and Trust to serve as the parent company for both our United States and Canadian commercial finance companies.

We discuss this line of business further in the Commercial Finance section of the MD&A of this report.

Venture Capital

We re-entered the private equity business in late 1997 and established this line of business when we formed Irwin Ventures Incorporated in August 1999. Our objective is to make minority investments in early stage companies in the financial services industry and related fields that intend to use technology as a key component of their competitive strategies. We provide Irwin Ventures portfolio companies the benefit of our management experience in the financial services industry. In addition, we expect that contacts made through venture activities may benefit management of our other lines of business through the sharing of technologies and market opportunities.

In April 2000, Irwin Ventures established a subsidiary, Irwin Ventures Incorporated-SBIC, which received a small business investment company license from the Small Business Administration. In December 2000, Irwin Ventures and Irwin Ventures-SBIC became Delaware limited liability companies. To date, the primary geographic focus of this line of business and each of our investments has been on the corridors of the east and west coasts between Washington, D.C. and Boston, and Palo Alto and Seattle.

Since inception we have invested $14.7 million in eight portfolio companies. However, over the last two years we have found it more difficult to find new investments that meet our strategic objectives and have re-directed certain personnel formerly addressing this segment. In 2004 and 2003, only $0.1 million and $2.0 million, respectively were invested in portfolio companies. In addition, our growth has caused this activity to become less significant on a consolidated basis. When the company was formed, we expected to make approximately $4 million in annual investments. That was 2.5% of year-end 1999 common equity. We now expect that annual investments are unlikely to exceed $2 million which would be less than 0.4% of 2004 year-end common equity.

Given the change in the materiality of this segment to consolidated results, we intend to discontinue segment reporting for private equity with this report. When appropriate due to materiality, we will report on financial results for private equity in the Parent and Other segment.

Customer Base

No single part of our business is dependent upon a single customer or upon a very few customers and the loss of any one customer would not have a materially adverse effect upon our business.

Competition

We compete nationally in the U.S. in each business, except for commercial banking where our market focus is in the Midwest and Rocky Mountain states, and for commercial leasing where products are offered in the U.S. and throughout Canada. In our mortgage banking business we compete for mortgage loans with

mortgage banking companies, as well as commercial banks, savings banks, credit unions and savings and loan associations, and with a number of nonbank companies.

In our home equity lending business, our primary competitors for our home equity loans and lines of credit are similar to those in our mortgage banking business with the addition of large securities firms, credit card issuers and finance companies. Competitors in our commercial banking business include all of the above institutions.

In our venture capital line of business, we compete primarily with other venture capital firms that invest in start-up companies.

Some of our competitors are not subject to the same degree of regulation as that imposed on bank holding companies, state banking organizations and federal saving banks. In addition, many larger banking organizations, mortgage companies, mortgage banks, insurance companies and securities firms have significantly greater resources than we do. As a result, some of our competitors have advantages over us in name recognition and market penetration.

Financial Information About Geographic Areas

We conduct part of our commercial finance line of business in Canadian markets. Net revenues for the last three years in this line of business attributable to Canadian customers were $11.5 million, $7.9 million and $5.2 million in 2004, 2003 and 2002, respectively.

Supervision and Regulation

General

The financial services business is highly regulated, primarily for the protection of depositors and other customers. The following is a summary of several applicable statutes and regulations that apply to us and to our subsidiaries. These summaries are not complete, and you should refer to the statutes and regulations for more information. Also, these statutes and regulations may change in the future, and we cannot predict what effect these changes, if made, will have on our operations.

We are regulated at both the holding company and subsidiary level and subject to both state and federal regulation and examinations relating to safety and soundness, including risk management, asset quality and capital adequacy, as well as a broad range of other regulatory concerns including: insider transactions, the adequacy of the reserve for loan losses, intercompany transactions, regulatory reporting, adequacy of systems of internal controls and limitations on permissible activities.

Our product and service offerings are subject to a number of consumer protection laws and regulations. In many instances these rules contain specific requirements regarding the content and timing of disclosures and the manner in which we must process and execute transactions. Some of these rules provide consumers with rights and remedies, including the right to initiate private litigation.

In addition, financial services providers are required to establish and administer a variety of processes and programs to address other regulatory requirements, including: community reinvestment provisions; protection of customer information; identification of suspicious activities, including possible money laundering; proper identification of customers when performing transactions; maintenance of information and site security; and other bank compliance provisions. In a number of instances board and/or management oversight is required as well as employee training on specific regulations.

Regulatory agencies have a broad range of sanctions and enforcement powers, including civil money penalties, formal agreements, and cease and desist orders.

Bank Holding Company Regulation

We are registered as a bank holding company with the Board of Governors of the Federal Reserve System under the Bank Holding Company Act of 1956, as amended and the related regulations, referred to as the

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BHC Act. We are subject to regulation, supervision and examination by the Federal Reserve, and as part of this process, we must file reports and additional information with the Federal Reserve.

Minimum Capital Requirements

The Federal Reserve has adopted risk-based capital guidelines for assessing bank holding company capital adequacy. These standards define capital and establish minimum capital ratios in relation to assets, both on an aggregate basis and as adjusted for credit risks and off-balance sheet exposures. Under the Federal Reserve s risk-based guidelines applicable to us, capital is classified into two categories for bank holding companies:

Tier 1 capital, or core capital, consists of:

- common stockholder s equity;
- qualifying noncumulative perpetual preferred stock;
- qualifying cumulative perpetual preferred stock (subject to some limitations, and including our Trust Preferred securities, of which $165 million qualified as Tier 1 capital as of December 31, 2004); and
- minority interests in the common equity accounts of consolidated subsidiaries;

less

- goodwill;
- credit-enhancing interest-only strips (certain amounts only); and
- specified intangible assets (including $19 million of disqualified Mortgage Servicing Assets (MSRs) as of December 31, 2004).

Tier 2 capital, or supplementary capital, consists of:

- allowance for loan and lease losses;
- perpetual preferred stock and related surplus;
- hybrid capital instruments (including Trust Preferred securities, of which $67 million qualified as Tier 2 capital as of December 31, 2004);
- unrealized holding gains on equity securities;
- perpetual debt and mandatory convertible debt securities;
- term subordinated debt, including related surplus; and
- intermediate-term preferred stock, including related securities.

The Federal Reserve s capital adequacy guidelines require bank holding companies to maintain a minimum ratio of qualifying total capital to risk-weighted assets of 8 percent, at least 4 percent of which must be in the form of Tier 1 capital. Risk-weighted assets include assets and credit equivalent amounts of off-balance sheet items of bank holding companies that are assigned to one of several risk categories, based on the obligor or the nature of the collateral. The Federal Reserve has established a minimum ratio of Tier 1 capital (less any intangible capital items) to total assets (less any intangible assets), or leverage ratio, of 3 percent for strong bank holding companies (those rated a composite 1 under the Federal Reserve s rating system). For all other bank holding companies, the minimum ratio of Tier 1 capital to total assets is 4 percent. Also, the Federal Reserve continues to consider the Tier 1 leverage ratio in evaluating proposals for expansion or new activities.

In its capital adequacy guidelines, the Federal Reserve emphasizes that the standards discussed above are minimums and that banking organizations generally are expected to operate well above these minimum levels. These guidelines also state that banking organizations

experiencing growth, whether internally or through

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acquisitions or other expansionary initiatives, are expected to maintain strong capital positions substantially above the minimum levels.

As of December 31, 2004, we had regulatory capital in excess of all the Federal Reserve s minimum levels and our internal minimum target of 11% for risk-adjusted capital. Our ratio of total capital to risk weighted assets at December 31, 2004 was 15.9% and our Tier 1 leverage ratio was 11.6%.

Expansion

The BHC Act requires prior Federal Reserve approval for certain activities, such as the acquisition by a bank holding company of more than 5% of the voting shares of any company, including a bank or bank holding company. Under the BHC Act, a bank holding company may engage in activities that the Federal Reserve has determined to be so closely related to banking or managing or controlling banks as to be a proper incident to those banking activities, such as operating a mortgage bank or a savings association, conducting leasing and venture capital investment activities, performing trust company functions, or acting as an investment or financial advisor. See the section on Interstate Banking and Branching below.

Dividends

The Federal Reserve has policies on the payment of cash dividends by bank holding companies. The Federal Reserve believes that a bank holding company experiencing earnings weaknesses should not pay cash dividends (1) exceeding its net income or (2) which only could be funded in ways that would weaken a bank holding company s financial health, such as by borrowing. Also, the Federal Reserve possesses enforcement powers over bank holding companies and their non-bank subsidiaries to prevent or remedy unsafe or unsound practices or violations of applicable statutes and regulations. Among these powers is the ability to prohibit or limit the payment of dividends by banks (including dividends to bank holding companies) and bank holding companies. See Dividend Limitations below.

The Federal Reserve expects us to act as a source of financial strength to our banking subsidiaries and to commit resources to support them. In implementing this policy, the Federal Reserve could require us to provide financial support when we otherwise would not consider ourselves able to do so.

In addition to the restrictions on fundamental corporate actions such as acquisitions and dividends imposed by the Federal Reserve, Indiana law also places limitations on our authority with respect to such activities.

Sarbanes-Oxley Act of 2002

The Sarbanes-Oxley Act of 2002 comprehensively revised the laws affecting corporate governance, accounting obligations and corporate reporting for companies, including us, that have equity or debt securities registered under the Securities Exchange Act of 1934. In particular, the Sarbanes-Oxley Act established: (i) new requirements for audit committees, including independence, expertise, and responsibilities; (ii) additional responsibilities regarding financial statements for the Chief Executive Officer and Chief Financial Officer of the reporting company; (iii) new standards for auditors and regulation of audits; (iv) increased disclosure and reporting obligations for the reporting company and its directors and executive officers; and (v) new and increased civil and criminal penalties for violation of the securities laws.

Bank and Thrift Regulation

Indiana law subjects Irwin Union Bank and Trust and its subsidiaries to supervision and examination by the Indiana Department of Financial Institutions. Irwin Union Bank and Trust is a member of the Federal Reserve System and, along with its subsidiaries, is also subject to regulation, examination and supervision by the Federal Reserve. Subsidiaries routinely subject to examination include Irwin Mortgage, Irwin Home Equity and Irwin Commercial Finance.

Irwin Union Bank, F.S.B., a direct subsidiary of the bank holding company, is a federally chartered savings bank. Accordingly, it is governed by and subject to regulation, examination and supervision by the Office of Thrift Supervision (OTS).

The Federal Reserve also supervises Irwin Union Bank and Trust s compliance with federal law and regulations that restrict loans by member banks to their directors, executive officers, and other controlling persons, as well as transactions with affiliated entities. The OTS supervises Irwin Union Bank, F.S.B, s compliance with these laws and regulations.

The deposits of Irwin Union Bank and Trust are insured by the Bank Insurance Fund and the deposits of Irwin Union Bank, F.S.B. are insured by the Savings Association Insurance Fund under the provisions of the Federal Deposit Insurance Act (FDIA). As a result, Irwin Union Bank and Trust and Irwin Union Bank, F.S.B. are subject to supervision and examination by the Federal Deposit Insurance Corporation (FDIC).

Irwin Union Bank and Trust and Irwin Union Bank, F.S.B. must file reports with the Federal Reserve and the OTS, respectively, and with the FDIC concerning its activities and financial condition in addition to obtaining regulatory approvals before establishing branches or entering into certain transactions such as mergers with, or acquisitions of, other financial institutions.

Mortgage Banking and Residential Lending Regulation

The residential lending activities of Irwin Union Bank and Trust, the mortgage banking activities of its subsidiary, Irwin Mortgage, and the home equity lending business of Irwin Union Bank and Trust s subsidiary Irwin Home Equity, are regulated by the Federal Reserve. The Federal Reserve has broad authority to oversee the banking activities of Irwin Union Bank and Trust and its subsidiaries as the primary federal regulator of the bank, pursuant to the Federal Reserve Act, and the nonbanking subsidiaries of Irwin Financial Corporation, pursuant to the BHC Act. Federal Reserve regulations and policies, such as restrictions on affiliate transactions and real estate lending policies relating to asset quality and prudent underwriting of loans, apply to our residential lending activities. The Indiana Department of Financial Institutions has comparable supervisory and examination authority over Irwin Mortgage, Irwin Home Equity and Irwin Commercial Finance due to their status as subsidiaries of Irwin Union Bank and Trust.

Capital Requirements

The Federal Reserve has published regulations applicable to state member banks such as Irwin Union Bank and Trust regarding the maintenance of adequate capital substantially similar to the capital regulations applicable to bank holding companies described in the section on *Bank Holding Company Regulation Minimum Capital Requirements.* While retaining the authority to set capital ratios for individual banks, these regulations prescribe minimum total risk-based capital, Tier 1 risk-based capital and leverage (Tier 1 capital divided by average total assets) ratios. The Federal Reserve requires banks to hold capital commensurate with the level and nature of all of the risks, including the volume and severity of problem loans, to which they are exposed.

As with the regulations applicable to bank holding companies, the Federal Reserve requires all state member banks to meet a minimum ratio of qualifying total capital to weighted risk assets of 8 percent, of which at least 4 percent should be in the form of Tier 1 capital.

The minimum ratio of Tier 1 capital to total assets, or the leverage ratio, for strong banking institutions (rated composite 1 under the uniform rating system of banks) is 3 percent. For all other institutions, the minimum ratio of Tier 1 capital to total assets is 4 percent. Banking institutions with supervisory, financial, operational, or managerial weaknesses are expected to maintain capital ratios well above the minimum levels, as are institutions with high or inordinate levels of risk. Banks experiencing or anticipating significant growth are also expected to maintain capital, including tangible capital positions, well above the minimum levels. A majority of such institutions generally have operated at capital levels ranging from 1 to 2 percent above the stated minimums. Higher capital ratios could be required if warranted by the particular circumstances to risk profiles of individual banks. The standards set forth above specify minimum supervisory ratios based primarily

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on broad credit risk considerations. The risk-based ratio does not take explicit account of the quality of individual asset portfolios or the range of other types of risks to which banks may be exposed, such as interest rate, liquidity, market or operational risks. For this reason, banks are generally expected to operate with capital positions above the minimum ratios.

At December 31, 2004, Irwin Union Bank and Trust had a total risk-based capital ratio of 14.6%, a Tier 1 capital ratio of 13.0%, and a leverage ratio of 11.3%.

The Federal Reserve, the OTS, the FDIC and other federal banking agencies also adopted a rule modifying the risk-based capital standards to provide for consideration of interest rate risk when assessing capital adequacy of a bank or savings association. Under this rule, the Federal Reserve, the OTS and the FDIC must explicitly include a bank or savings association s exposure to declines in the economic value of their capital due to changes in interest rates as a factor in evaluating capital adequacy of a bank or savings association. This assessment of interest rate risk management made by the banks examiners is incorporated into the banks overall risk management rating and used to determine management s effectiveness.

Insurance of Deposit Accounts

As FDIC-insured institutions, Irwin Union Bank and Trust and Irwin Union Bank, F.S.B. are required to pay deposit insurance premiums based on the risk they pose to the Bank Insurance Fund (BIF) and the Savings Association Insurance Fund (SAIF), respectively. Currently, the amount of FDIC assessments paid by an insured depository institution ranges from zero to $0.27 per $100 of insured deposits, based on the institution s relative risk to the deposit insurance funds, as measured by the institution s regulatory capital position and other supervisory factors. The FDIC also has the authority to raise or lower assessment rates on insured deposits to achieve the statutorily required reserve ratios in insurance funds and to impose special additional assessments.

In addition to deposit insurance fund assessments, the FDIC assesses both BIF and SAIF insured deposits a special assessment to fund the repayment of debt obligations of the Financing Corporation (FICO). FICO is a government-sponsored entity that was formed to borrow the money necessary to carry out the closing and ultimate disposition of failed thrift institutions by the Resolution Trust Corporation. At December 31, 2004, the annualized rate established by the FDIC for the FICO assessment on both BIF and SAIF deposits was 1.46 basis points per $100 of insured deposits.

Dividend Limitations

As a state member bank, Irwin Union Bank and Trust may not, without the approval of the Federal Reserve, declare a dividend if the total of all dividends declared in a calendar year, including the proposed dividend, exceeds the total of its net income for that year, combined with its retained net income of the preceding two years, less any required transfers to the surplus account. Under Indiana law, certain dividends require notice to, or approval by, the Indiana Department of Financial Institutions, and Irwin Union Bank and Trust may not pay dividends in an amount greater than its net profits then available, after deducting losses and bad debts.

In most cases, savings and loan associations, such as Irwin Union Bank, F.S.B., are required either to apply to or to provide notice to the OTS regarding the payment of dividends. The savings association must seek approval if it does not qualify for expedited treatment under OTS regulations, or if the total amount of all capital distributions for the applicable calendar year exceeds net income for that year to date plus retained net income for the preceding two years, or the savings association would not be adequately capitalized following the dividend, or the proposed dividend would violate a prohibition in any statute, regulation or agreement with the OTS. In other circumstances, a simple notice is sufficient.

Our ability and the ability of Irwin Union Bank and Trust and Irwin Union Bank, F.S.B. to pay dividends also may be affected by the various capital requirements and the capital and noncapital standards established under the FDICIA, as described above. Our rights and the rights of our shareholders and our creditors to

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participate in any distribution of the assets or earnings of our subsidiaries also is subject to the prior claims of creditors of our subsidiaries including the depositors of a bank subsidiary.

Interstate Banking and Branching

Under the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (the Interstate Banking Act), banks are permitted, subject to being adequately or better capitalized, in compliance with Community Reinvestment Act requirements and in compliance with state law requirements (such as age-of-bank limits and deposit caps), to merge with one another across state lines and to create a main bank with branches in separate states. After establishing branches in a state through an interstate merger transaction, a bank may establish and acquire additional branches at any location in the state where any bank involved in the interstate merger could have established or acquired branches under applicable federal and state law.

As a federally chartered savings bank, Irwin Union Bank, F.S.B. has greater flexibility in pursuing interstate branching than an Indiana state bank. Subject to certain exceptions, a federal savings association generally may establish or operate a branch in any state outside the state of its home office if the association meets applicable statutory requirements.

Community Reinvestment

Under the Community Reinvestment Act (CRA), banking and thrift institutions have a continuing and affirmative obligation, consistent with their safe and sound operation, to help meet the credit needs of their entire communities, including low- and moderate-income neighborhoods. The CRA does not establish specific lending requirements or programs for financial institutions, or limit an institution s discretion to develop the types of products and services it believes are best suited to its particular community that are consistent with the CRA. Institutions are rated on their performance in meeting the needs of their communities. Performance is tested in three areas: (a) lending, which evaluates the institution s record of making loans in its assessment areas; (b) investment, which evaluates the institution s record of investing in community development projects, affordable housing and programs benefiting low or moderate income individuals and business; and (c) service, which evaluates the institution s delivery of services through its branches, ATMs and other activities. The CRA requires each federal banking agency, in connection with its examination of a financial institution, to assess and assign one of four ratings to the institution s record of meeting the credit needs of its community and to take this record into account in evaluating certain applications by the institution, including applications for charters, branches and other deposit facilities, relocations, mergers, consolidations, acquisitions of assets or assumptions of liabilities, and savings and loan holding company acquisitions. The CRA also requires that all institutions publicly disclose their CRA ratings. Both Irwin Union Bank and Trust and Irwin Union Bank, F.S.B. received a satisfactory rating on their most recent CRA performance evaluations.

Other Safety and Soundness Regulations

Under current law, the federal banking agencies possess broad powers to take prompt corrective action in connection with depository institutions and their bank holding companies that do not meet minimum capital requirements. The law establishes five capital categories for insured depository institutions for this purpose: well-capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized. To be considered well-capitalized under these standards, an institution must maintain a total risk-based capital ratio of 10% or greater; a Tier 1 risk-based capital ratio of 6% or greater; a leverage capital ratio of 5% or greater; and not be subject to any order or written directive to meet and maintain a specific capital level for any capital measure. An adequately capitalized institution must have a Tier 1 capital ratio of at least 4%, a total capital ratio of at least 8% and a leverage ratio of at least 4%. Federal law also requires the bank regulatory agencies to implement systems for prompt corrective action for institutions that fail to meet minimum capital requirements within the five capital categories, with progressively more severe restrictions on operations, management and capital distributions according to the category in which an institution is placed. Failure to meet capital requirements can also cause an institution to be directed to raise additional capital. Federal law also mandates that the agencies adopt safety and soundness standards relating

generally to operations and management, asset quality and executive compensation, and authorizes administrative action against an institution that fails to meet such standards.

Brokered Deposits

Brokered deposits include funds obtained, directly or indirectly, by or through a deposit broker for deposit into one or more deposit accounts. Well-capitalized institutions are not subject to limitations on brokered deposits, while an adequately capitalized institution is able to accept, renew or rollover brokered deposits only with a waiver from the FDIC and subject to certain restrictions on the yield paid on such deposits. Undercapitalized institutions are not permitted to accept brokered deposits. Irwin Union Bank and Trust and Irwin Union Bank, F.S.B. are permitted to accept brokered deposits.

Gramm-Leach-Bliley Act

In 1999, the Gramm-Leach-Bliley Act (the GLB Act) amended or repealed certain provisions of the Glass-Steagall Act and other legislation that restricted the ability of bank holding companies, securities firms and insurance companies to affiliate with one another. The GLB Act established a comprehensive framework to permit affiliations among commercial banks, insurance companies and securities firms. The GLB Act also contains provisions intended to safeguard consumer financial information in the hands of financial service providers by, among other things, requiring these entities to share their privacy policies with their customers and allowing customers to opt out of having their financial service providers disclose their confidential financial information with non-affiliated third parties, subject to certain exceptions. Financial privacy regulations implementing the GLB provisions contain specific provisions on the treatment and safeguarding of confidential financial information. To the extent the GLB Act permits banks, securities firms and insurance companies to affiliate, the financial services industry may experience further consolidation. This consolidation could result in a growing number of larger financial institutions that offer a wider variety of financial services than we currently offer and that can aggressively compete in the markets we currently serve.

Anti-Money Laundering Laws

Irwin Union Bank and Trust and Irwin Union Bank, F.S.B. are subject to the Bank Secrecy Act and its implementing regulations and other anti-money laundering laws and regulations, including the USA PATRIOT Act of 2001. Among other things, these laws and regulations require Irwin Union Bank and Trust and Irwin Union Bank F.S.B to take steps to prevent the use of each institution for facilitating the flow of illegal or illicit money, to report large currency transactions and to file suspicious activity reports. Each bank also is required to develop and implement a comprehensive anti-money laundering compliance program. Banks also must have in place appropriate know your customer policies and procedures. Violations of these requirements can result in substantial civil and criminal sanctions. In addition, provisions of the USA PATRIOT Act require the federal financial institution regulatory agencies to consider the effectiveness of a financial institution s anti-money laundering activities when reviewing bank mergers and bank holding company acquisitions.

Compliance with Consumer Protection Laws

Our subsidiaries also are subject to many federal and state consumer protection statutes and regulations including the Equal Credit Opportunity Act, the Fair Housing Act, the Truth in Lending Act, the Truth in Savings Act, the Real Estate Settlement Procedures Act and the Home Mortgage Disclosure Act. Among other things, these acts:

- require lenders to disclose credit terms in meaningful and consistent ways;
- prohibit discrimination against an applicant in any consumer or business credit transaction;
- prohibit discrimination in housing-related lending activities;
- require certain lenders to collect and report applicant and borrower data regarding loans for home purchases or improvement projects;

- require lenders to provide borrowers with information regarding the nature and cost of real estate settlements;
- prohibit certain lending practices and limit escrow account amounts with respect to real estate transactions; and
- prescribe possible penalties for violations of the requirements of consumer protection statutes and regulations.

In addition, banking subsidiaries are subject to a number of regulations that offer consumer protections to depositors, including account terms and disclosures, funds availability and electronic funds transfers.

Equal Credit Opportunity Act

The federal Equal Credit Opportunity Act prohibits discrimination against an applicant in any credit transaction, whether for consumer or business purposes, on the basis of race, color, religion, national origin, sex, marital status, age (except in limited circumstances), receipt of income from public assistance programs or good faith exercise of any rights under the Consumer Credit Protection Act. In addition to prohibiting outright discrimination on any of the impermissible bases listed above, an effects test has been applied to determine whether a violation of the act has occurred. This means that if a creditor s actions have had the effect of discriminating, the creditor may be held liable, even when there is no intent to discriminate. In addition to actual damages, the Equal Credit Opportunity Act permits regulatory agencies to take enforcement action and provides for punitive damages. Successful complainants also may be entitled to an award of court costs and attorneys fees.

Fair Housing Act

The federal Fair Housing Act regulates many lending practices, including prohibiting discrimination in a lender s housing-related lending activities against any person because of race, color, religion, national origin, sex, handicap or familial status. The Fair Housing Act is broadly written and has been broadly interpreted by the courts. A number of lending practices have been found to be, or may be considered, illegal under the Fair Housing Act, including some that are not specifically mentioned in the act itself. Among those practices that have been found to be, or may be considered, illegal under the Fair Housing Act are declining a loan for the purposes of racial discrimination, making excessively low appraisals of property based on racial considerations and pressuring, discouraging, or denying applications for credit on a prohibited basis.

The Fair Housing Act allows a person who believes he or she has been discriminated against to file a complaint with the Department of Housing and Urban Development (HUD). Aggrieved persons also may initiate a civil action. The Fair Housing Act also permits the Attorney General of the United States to commence a civil action if there is reasonable cause to believe that a person has been discriminated against in violation of the Fair Housing Act. Penalties for violation of the Fair Housing Act include actual damages suffered by the aggrieved person and injunctive or other equitable relief. The courts also may assess civil penalties.

Home Mortgage Disclosure Act

The federal Home Mortgage Disclosure Act grew out of public concern over the availability of credit in certain urban neighborhoods. One purpose of the Home Mortgage Disclosure Act is to provide public information that will help show whether financial institutions are serving the housing credit needs of the neighborhoods and communities in which they are located. The Home Mortgage Disclosure Act also includes a fair lending aspect that requires the collection and disclosure of data about applicant and borrower characteristics as a way of identifying possible discriminatory lending patterns and enforcing anti-discrimination statutes. The Home Mortgage Disclosure Act requires institutions to report data regarding applications for loans for the purchase or improvement of one-to-four family and multifamily dwellings, as well as information concerning originations and purchases of such loans. Federal bank regulators rely, in part, upon

data provided under the Home Mortgage Disclosure Act to determine whether depository institutions engage in discriminatory lending practices.

The appropriate federal banking agency (that is, the Federal Reserve for Irwin Union Bank and Trust and the OTS for Irwin Union Bank, F.S.B.), or in some cases, HUD, enforces compliance with the Home Mortgage Disclosure Act and implements its regulations. Administrative sanctions, including civil money penalties, may be imposed by supervisory agencies for violations of this act.

Real Estate Settlement Procedures Act

The federal Real Estate Settlement Procedures Act (RESPA), requires lenders to provide borrowers with disclosures regarding the nature and cost of real estate settlements. RESPA also prohibits certain abusive practices, such as kickbacks, and places limitations on the amount of escrow accounts. Violations of RESPA may result in imposition of penalties, including: (1) civil liability equal to three times the amount of any charge paid for the settlement services or civil liability of up to $1,000 per claimant, depending on the violation; (2) awards of court costs and attorneys fees; and (3) fines of not more than $10,000 or imprisonment for not more than one year, or both. A significant number of individual claims and purported consumer class action claims have been commenced against financial institutions and other mortgage lending companies, including Irwin Mortgage, alleging violations of the prohibition against kickbacks and seeking civil damages, court costs and attorneys fees. See the Legal Proceedings section of this report.

Truth in Lending Act

The federal Truth in Lending Act is designed to ensure that credit terms are disclosed in a meaningful way so that consumers may compare credit terms more readily and knowledgeably. As a result of the act, all creditors must use the same credit terminology and expressions of rates, the annual percentage rate, the finance charge, the amount financed, the total of payments and the payment schedule.

Violations of the Truth in Lending Act may result in regulatory sanctions and in the imposition of both civil and, in the case of willful violations, criminal penalties. Under certain circumstances, the Truth in Lending Act and Federal Reserve Regulation Z also provide a consumer with a right of rescission, which relieves the consumer of the obligation to pay amounts to the creditor or to a third party in connection with the offending transaction, including finance charges, application fee, commitment fees, title search fees and appraisal fees. Consumers may also seek actual and punitive damages for violations in the Truth in Lending Act. See the Legal Proceedings section of this report.

State Consumer Protection Laws

In addition to the federal consumer protection laws discussed above, our subsidiaries are also subject to state consumer protection laws that regulate the mortgage origination and lending businesses of these subsidiaries. As part of the home equity line of business in conjunction with its subsidiary, Irwin Home Equity, Irwin Union Bank and Trust originates home equity loans through its branch in Carson City, Nevada. Irwin Union Bank and Trust uses interest rates and loan terms in its home equity loans and lines of credit that are authorized by Nevada law, but might not be authorized by the laws of the states in which the borrowers are located. As a FDIC-insured, state member bank, Irwin Union Bank and Trust is authorized by Section 27 of the FDIA to charge interest at rates allowed by the laws of the state where the bank is located regardless of any inconsistent state law, and to apply these rates to loans to borrowers in other states. The FDIC has opined that a state bank with branches outside of the state in which it is chartered may also be located in a state in which it maintains an interstate branch. Irwin Union Bank and Trust relies on Section 27 of the FDIA and the FDIC opinion in conducting its home equity lending business described above. From time to time, state regulators have questioned the application of Section 27 of the FDIA to credit practices affecting citizens of their states. Any change in Section 27 of the FDIA or in the FDIC s interpretation of this provision, or any successful challenge as to the permissibility of these activities, could require that we change the terms of some of our loans or the manner in which we conduct our home equity line of business.

Employees and Labor Relations

At January 31, 2005, we and our subsidiaries had a total of 3,145 employees, including full-time and part-time employees. We continue a commitment of equal employment opportunity for all job applicants and staff members, and management regards its relations with its employees as satisfactory.

Executive Officers

Our executive officers are elected annually by the Board of Directors and serve for a term of one year or until their successors are elected and qualified. In addition to our Chairman and Chief Executive Officer, Mr. William I. Miller (48), who also serves as a director, our executive officers are listed below.

Richard Barbercheck (46) has been Vice President-Corporate Credit Risk Evaluation Officer since October 2003. He was an officer of Irwin Union Bank and Trust since March 1998.

Elena Delgado (49) has been President and Chief Executive Officer of Irwin Home Equity since September 1994.

Gregory F. Ehlinger (42) has been our Senior Vice President and Chief Financial Officer since August of 1999. He has been one of our officers since August 1992.

Paul D. Freudenthaler (40) has been our Vice President-Chief Risk Officer since December 2003. He was Vice President-Financial Risk Management from December 2001 to December 2003. From September 2000 through November 2001, he was Corporate Controller for America Online Latin America, an Internet service provider. From July 2000 to August 2000 he served as Senior Vice President-Treasurer of Telscape International, Inc., a development stage telecommunications company. Prior thereto, he held the position of Chief Accounting Officer of Telscape from July 1999 until June 2000. Subsequent to his departure from Telscape, Telscape filed a voluntary petition for relief under Chapter 11 of the U.S. Bankruptcy Code on April 27, 2001. From February 1999 through June 1999, he was Director-International of Bank United, F.S.B. From January 1994 through January 1999, he was Director-International of Irwin Mortgage Corporation, our subsidiary.

Jose M. Gonzalez (46) has been our Vice President-Director Internal Audit since October 1995.

Robert H. Griffith (46) has been President and Chief Executive Officer of Irwin Mortgage since January 2001. He has been an officer of Irwin Mortgage since 1993.

Bradley J. Kime (44) has been President of Irwin Union Bank s commercial line of business since May 2003. He has been President of Irwin Union Bank F.S.B. since December 2000. He has been an officer of Irwin Union Bank and Trust since 1987 and one of our officers since 1986.

Joseph R. LaLeggia (43) has been President of Irwin Commercial Finance Corporation since July of 2002. He has been the President and Chief Executive Officer of Irwin Commercial Finance Canada Corporation (formerly, Onset Capital Corporation) since April 1998. From January 1997 until April of 1998 he was President of AT&T Capital Canada Inc.

Matthew F. Souza (48) has been our Senior Vice President-Ethics since August 1999 and our Secretary since 1986. He has been one of our officers since 1986.

Thomas D. Washburn (58) has been our Executive Vice President since August 1999 and one of our officers since 1976. From 1981 to August 1999 he served as our Senior Vice President and Chief Financial Officer.

Item 2. *Properties*

Our main office and the main offices of Irwin Ventures LLC are located at 500 Washington Street, Columbus, Indiana, in space leased from Irwin Union Bank and Trust. The location and general character of our other materially important physical properties as of January 31, 2005 are as follows:

Irwin Mortgage

The main office, where administrative and servicing activities are centered, is located at 10500 Kincaid Drive, Fishers, Indiana, and is leased. Loan production and satellite offices, which are leased, are operated from approximately 169 locations in 33 states.

Irwin Union Bank and Trust

The main office is located in four buildings at 435, 500, 520 and 526 Washington Street, Columbus, Indiana. Irwin Union Realty Corporation, a wholly-owned subsidiary of Irwin Union Bank and Trust, owns these buildings in fee and leases them to Irwin Union Bank and Trust. One or the other of Irwin Union Bank and Trust or Irwin Union Realty owns the branch properties in fee at six locations in Columbus. These properties have no major encumbrances. Irwin Union Bank and Trust leases eleven other branch offices in Central and Southern Indiana, four offices in Michigan, two offices in Nevada, and one in Utah.

Irwin Union Bank, F.S.B.

The main office is located at 140 Whittington Parkway, Suite 100, Louisville, Kentucky. Irwin Union Bank, F.S.B. has four branch offices located in Arizona, California, Missouri, and Wisconsin. All offices are leased.

Irwin Home Equity

The main office is located at 12677 Alcosta Boulevard, Suite 500, San Ramon, California. Irwin Home Equity also occupies one other office at this location in San Ramon, California. Both offices are leased.

Irwin Commercial Finance Corporation

The main office of Irwin Commercial Finance Corporation is located at 500 Washington Street, Columbus, Indiana. The office of our domestic commercial finance operation, Irwin Business Finance Corporation is located at 330 120th Avenue NE, Bellevue, Washington and is leased. Our Canadian commercial finance subsidiary, Irwin Commercial Finance Canada Corporation (formerly Onset Capital Corporation), leases its main office at Suite 300 Park Place, 666 Burrard Street, Vancouver, British Columbia, Canada, and leases its three processing centers in Calgary, Alberta; Toronto, Ontario; and Montreal, Quebec. The main offices of our franchise lending subsidiary, Irwin Franchise Capital Corporation, are located at 10 Paragon Drive, Montvale, New Jersey and 2700 Westchester Avenue, Purchase, New York and are both leased. In addition, Irwin Franchise Capital owns the building that houses its telesales center at 2715 13th Street, Columbus, Nebraska.

Item 3. *Legal Proceedings*

Culpepper v. Inland Mortgage Corporation

Our indirect subsidiary, Irwin Mortgage Corporation (formerly Inland Mortgage Corporation), is a defendant in a class action lawsuit in the United States District Court for the Northern District of Alabama, filed in April 1996, alleging that Irwin Mortgage violated the federal Real Estate Settlement Procedures Act (RESPA) relating to Irwin Mortgage s payment of broker fees to mortgage brokers. In June 2001, the Court of Appeals for the 11th Circuit upheld the district court s certification of a plaintiff class and the case was remanded for further proceedings in the federal district court.

In November 2001, by order of the district court, the parties filed supplemental briefs analyzing the impact of an October 18, 2001 policy statement issued by the Department of Housing and Urban Development (HUD) that explicitly disagreed with the judicial interpretation of RESPA by the Court of Appeals for the 11th Circuit in its ruling upholding class certification in this case. In response to a motion from Irwin Mortgage, in March 2002, the district court granted Irwin Mortgage s motion to stay proceedings in this case until the 11th Circuit decided the three other RESPA cases originally argued before it with this case.

The 11th Circuit subsequently decided all of the RESPA cases pending in that court. In one of those cases, the 11th Circuit concluded that the trial court had abused its discretion in certifying a class action under RESPA. Further, in that decision, the 11th Circuit expressly recognized it was, in effect, overruling its previous decision upholding class certification in our case. In March 2003, Irwin Mortgage filed a motion to decertify the class and the plaintiffs filed a renewed motion for summary judgment. On October 2, 2003 the case was reassigned to another U.S. district court judge. In response to an order from the court, the parties met and submitted a joint status report at the end of October 2003. On June 14, 2004, at the court s request, the parties engaged in mediation, which was unsuccessful. The court then reassigned this case to a new judge.

If the class is not decertified and the district court finds that Irwin Mortgage violated RESPA, Irwin Mortgage could be liable for damages equal to three times the amount of that portion of payments made to the mortgage brokers that is ruled unlawful. Based on notices sent by the plaintiffs to date to potential class members and additional notices that might be sent in this case, we believe the class is not likely to exceed 32,000 borrowers who meet the class specifications.

Irwin Mortgage intends to defend this lawsuit vigorously and believes it has numerous defenses to the alleged violations. Irwin Mortgage further believes that the 11th Circuit s RESPA rulings in the cases argued before it with this one provide grounds for reversal of the class certification in this case. We have no assurance, however, that Irwin Mortgage will be successful in defeating class certification or will ultimately prevail on the merits. However, we expect that an adverse outcome in this case could result in substantial monetary damages that could be material to our financial position. We have not established any reserves for this case and are unable at this stage of the litigation to form a reasonable estimate of potential loss that we could suffer.

United States ex rel. Paranich v. Sorgnard et al.

In January 2001, we and Irwin Leasing Corporation (formerly Affiliated Capital Corp.), our indirect subsidiary, and Irwin Equipment Finance Corporation, our direct subsidiary (together, the Irwin companies), were served as defendants in an action filed in the United States District Court for the Middle District of Pennsylvania. The suit alleges that a manufacturer/importer of certain medical devices made misrepresentations to health care professionals and to government officials to improperly obtain Medicare reimbursement for treatments using the devices, and that the Irwin companies, through Affiliated Capital s financing activities, aided in making the alleged misrepresentations. On August 10, 2001, the court dismissed Irwin Financial and Irwin Equipment Finance as defendants in the suit. The Irwin companies prevailed on a motion for summary judgment in the district court on October 8, 2003, and the plaintiff appealed. The Court of Appeals for the Third Circuit heard oral argument on plaintiff s appeal on September 27, 2004. On January 28, 2005, the court of appeals affirmed the district court s dismissal of plaintiff s action. The period for which the plaintiff can petition the United States Supreme Court for a writ of certiorari expires on April 28, 2005.

McIntosh v. Irwin Home Equity Corporation

Our subsidiary, Irwin Union Bank and Trust Company, was a defendant in a class action lawsuit filed in the United States District Court in Massachusetts in July 2001. The case involved loans purchased by Irwin Union Bank and Trust Company from an unaffiliated third-party originator. The plaintiffs alleged a failure to comply with certain disclosure provisions of the Truth in Lending Act relating to high-rate loans in making second mortgage home equity loans to the plaintiff borrowers. The complaint sought rescission of the loans and other damages.

A limited class was certified. As originally specified, the plaintiff class included those borrowers who obtained a mortgage loan originated by the third-party originator with prepayment penalty provisions during

the three-year period prior to the filing of the suit. Subsequently, the court further restricted the class to those borrowers with high-rate loans subject to the Home Ownership and Equity Protection Act who refinanced their loans and paid a prepayment penalty. A preliminary analysis led us to conclude that fewer than 100 loans qualified for class membership.

The parties settled this matter for a nonmaterial amount. The court dismissed the lawsuit with prejudice on December 16, 2004.

Stamper v. A Home of Your Own

Our indirect subsidiary, Irwin Mortgage Corporation, is a defendant in a case filed in August 1998 in the Baltimore, Maryland, City Circuit Court. On January 25, 2002, a jury in this case awarded the plaintiffs damages of $1.434 million jointly and severally against defendants, including Irwin Mortgage. The nine plaintiff borrowers alleged that a home rehabilitation company defrauded the plaintiffs by selling them defective homes at inflated prices and that Irwin Mortgage, which provided the plaintiff borrowers mortgage loans on the home purchases, participated in the fraud. Irwin Mortgage filed an appeal with the Maryland Court of Special Appeals and oral argument was held on January 7, 2003. On February 27, 2004, the Court of Special Appeals ruled against Irwin Mortgage and remanded the case to the trial court for a partial retrial on whether the plaintiffs are entitled to punitive damages. Irwin Mortgage petitioned the Maryland Court of Appeals for a writ of certiorari on April 12, 2004. The Court of Appeals granted Irwin Mortgage s petition and heard oral argument on November 4, 2004. On February 4, 2005, the Court of Appeals affirmed in part and reversed in part the judgment of the Court of Special Appeals, remanding the case as follows: to modify the judgment for all plaintiffs by striking the award of $145,000 for non-economic damages; for further proceedings concerning one plaintiff as to non-economic damages; and for a new trial as to punitive damages. We have reserved for this case based upon the advice of our legal counsel.

Silke v. Irwin Mortgage Corporation

In April 2003, our indirect subsidiary, Irwin Mortgage Corporation, was named as a defendant in a class action lawsuit filed in the Marion County, Indiana, Superior Court. The complaint alleges that Irwin Mortgage charged a document preparation fee in violation of Indiana law for services performed by clerical personnel in completing legal documents related to mortgage loans. Irwin Mortgage filed an answer on June 11, 2003 and a motion for summary judgment on October 27, 2003. On June 18, 2004, the court certified a plaintiff class consisting of Indiana borrowers who were allegedly charged the fee by Irwin Mortgage any time after April 17, 1997. This date was later clarified by stipulation of the parties to be April 14, 1997. We are unable at this time to form a reasonable estimate of the amount of potential loss, if any, that Irwin Mortgage could suffer. We have not established any reserves for this case.

Gutierrez v. Irwin Mortgage Corporation

In April 2003, our indirect subsidiary, Irwin Mortgage Corporation, was named as a defendant in an action filed in the District Court of Nueces County, Texas. The complaint alleged that Irwin Mortgage improperly charged borrowers fees for the services of third-party vendors in excess of Irwin Mortgage s costs, and charged certain fees to which plaintiffs did not agree. The plaintiffs sought to certify a class consisting of similarly situated borrowers. In August 2004, the plaintiffs amended their complaint to remove the allegations that Irwin Mortgage charged excess fees. After a period of discovery, the parties settled this case for a nonmaterial amount.

Cohens v. Inland Mortgage Corporation

In October 2003, our indirect subsidiary, Irwin Mortgage Corporation (formerly Inland Mortgage Corporation), was named as a defendant, along with others, in an action filed in the Supreme Court of New York, County of Kings. The plaintiffs, a mother and two children, allege they were injured from lead contamination while living in premises allegedly owned by the defendants. The suit seeks approximately $41 million in damages and alleges negligence, breach of implied warranty of habitability and fitness for

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intended use, loss of services and the cost of medical treatment. Because the case is in the early stages of litigation, we are unable at this time to form a reasonable estimate of the amount of potential loss, if any, that Irwin Mortgage could suffer. The parties agreed to delay the filing of an answer in this case until March 31, 2005. We are attempting to obtain a voluntary dismissal based on our belief that there is insufficient nexus between the cause of the alleged injuries and Irwin Mortgage. We have not established any reserves for this case.

Litigation in Connection with Loans Purchased from Community Bank of Northern Virginia

Our subsidiary, Irwin Union Bank and Trust Company, is a defendant in several actions in connection with loans Irwin Union Bank purchased from Community Bank of Northern Virginia (Community).

Hobson v. Irwin Union Bank and Trust Company was filed on July 30, 2004 in the United States District Court for the Northern District of Alabama. As amended on August 30, 2004, the *Hobson* complaint, seeks certification of both a plaintiffs and a defendants class, the plaintiffs class to consist of all persons who obtained loans from Community and whose loans were purchased by Irwin Union Bank. *Hobson* alleges that defendants violated the Truth-in-Lending Act (TILA), the Home Ownership and Equity Protection Act (HOEPA), the Real Estate Settlement Procedures Act (RESPA) and the Racketeer Influenced and Corrupt Organizations Act (RICO). On October 12, 2004, Irwin filed a motion to dismiss the *Hobson* claims as untimely filed and substantively defective.

Kossler v. Community Bank of Northern Virginia was originally filed in July 2002 in the United States District Court for the Western District of Pennsylvania. Irwin Union Bank and Trust was added as a defendant in December 2004. The *Kossler* complaint seeks certification of a plaintiffs class and seeks to void the mortgage loans as illegal contracts. Plaintiffs also seek recovery against Irwin for alleged RESPA violations and for conversion.

The plaintiffs in *Hobson* and *Kossler* claim that Community was allegedly engaged in a lending arrangement involving the use of its charter by certain third parties who charged high fees that were not representative of the services rendered and not properly disclosed as to the amount or recipient of the fees. The loans in question are allegedly high cost/high interest loans under Section 32 of HOEPA. Plaintiffs also allege illegal kickbacks and fee splitting. In *Hobson,* the plaintiffs allege that Irwin was aware of Community s alleged arrangement when Irwin purchased the loans and that Irwin participated in a RICO enterprise and conspiracy related to the loans. Because Irwin bought the loans from Community, the *Hobson* plaintiffs are alleging that Irwin has assignee liability under HOEPA.

If the *Hobson* and *Kossler* plaintiffs are successful in establishing a class and prevailing at trial, possible RESPA remedies could include treble damages for each service for which there was an unearned fee, kickback or overvalued service. Other possible damages in *Hobson* could include TILA remedies, such as rescission, actual damages, statutory damages not to exceed the lesser of $500,000 or 1% of the net worth of the creditor, and attorneys fees and costs; possible HOEPA remedies could include the refunding of all closing costs, finance charges and fees paid by the borrower; RICO remedies could include treble plaintiffs actually proved damages. In addition, the *Hobson* plaintiffs are seeking unspecified punitive damages. Under TILA, HOEPA, RESPA and RICO, statutory remedies include recovery of attorneys fees and costs. Other possible damages in *Kossler* could include the refunding of all origination fees paid by the plaintiffs.

Irwin Union Bank and Trust Company is also a defendant, along with Community, in two individual actions *(Chatfield v. Irwin Union Bank and Trust Company, et al.* and *Ransom v. Irwin Union Bank and Trust Company, et al.)* filed on June 9, 2004 in the Circuit Court of Frederick County, Maryland, involving mortgage loans Irwin Union Bank purchased from Community. On July 16, 2004, both of these lawsuits were removed to the United States District Court for the District of Maryland. The complaints allege that the plaintiffs did not receive disclosures required under HOEPA and TILA. The lawsuits also allege violations of Maryland law because the plaintiffs were allegedly charged or contracted for a prepayment penalty fee. Irwin believes the plaintiffs received the required disclosures and that Community, a Virginia-chartered bank, was permitted to charge prepayment fees to Maryland borrowers. Under the loan purchase agreements between

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Irwin and Community, Irwin has the right to demand repurchase of the mortgage loans and to seek indemnification from Community for the claims in these lawsuits.

Under the loan purchase agreement between Irwin and Community, Irwin has the right to demand repurchase of the mortgage loans and indemnification from Community for these claims. On September 17, 2004, Irwin made a demand for indemnification and a defense to *Hobson, Chatfield and Ransom.* Community denied this request as premature.

On December 22, 2004, Irwin filed a motion with the Judicial Panel On Multidistrict Litigation requesting a transfer of *Hobson, Chatfield* and *Ransom* to the Western District of Pennsylvania for coordinated or consolidated proceedings with the *Kossler* action. That motion was accepted by the Panel, and plaintiffs filed a motion in opposition.

At this early stage, we are unable to form a reasonable estimate of the amount of potential loss, if any, that Irwin could suffer. We have established a reserve for the Community litigation based upon the advice of legal counsel.

Litigation Related to NorVergence, Inc.

Irwin Business Finance, our indirect subsidiary, is involved on a national basis in equipment leasing finance and maintains a diverse portfolio of leases, including leases in the telecommunications field. A portion of Irwin s telecommunications portfolio involves leases of equipment acquired from NorVergence, Inc., a New Jersey-based telecommunications company. After assigning leases to Irwin and other lenders, NorVergence became a debtor in a Chapter 7 bankruptcy, which is currently pending in the United States Bankruptcy Court in New Jersey. The sudden failure of NorVergence left many of its customers without telecommunications service. These customers became very angry when commitments made to them by NorVergence went unfulfilled.

Complaints by former NorVergence customers have led to investigations by the Attorneys General of several states and the filing of a number of lawsuits. Irwin Business Finance has been named as a defendant in several lawsuits connected with NorVergence. *Exquisite Caterers, LLC et al. v. Popular Leasing et al.* is a lawsuit filed in the Superior Court of New Jersey, Monmouth County, and was amended to include Irwin Business Finance and others on September 1, 2004. The *Exquisite Caterers* plaintiffs seek certification of a class of persons who leased network computer equipment from NorVergence, whose leases were assigned to defendants. The complaint alleges that NorVergence misrepresented the services and equipment provided, that the lessees were defrauded and the lease agreements should not be enforced. The action alleges violations of, among other things, the New Jersey Consumer Fraud Act; the New Jersey Truth-in-Consumer Contract, Warranty, and Notice Act; the FTC Holder Rule; the FTC Act; and breach of contract and implied warranties. The plaintiffs seek compensatory, statutory and punitive damages, and injunctive relief, including rescission of the leases and cessation of collections.

Irwin Business Finance was also named as a defendant, along with other lenders, in *Delanco Board of Education et al. v. IFC Credit Corporation,* a lawsuit filed in the Superior Court of New Jersey, Essex County, Chancery Division, in October 2004 in connection with leases assigned to the lenders by NorVergence. (IFC Credit Corporation is not affiliated with Irwin Financial Corporation or Irwin Business Finance.) The suit involved more than one thousand plaintiffs and alleged fraud, misrepresentation and violations of the New Jersey Consumer Fraud law based on alleged conduct similar to that in *Exquisite Caterers,* with the addition of a count under the New Jersey RICO statute. Plaintiffs also alleged unjust enrichment and conversion and sought rescission of the leases plus punitive and other damages. After failing in an attempt to obtain a temporary injunction, the plaintiffs agreed to withdraw the complaint filed in the Superior Court and have now commenced actions in the NorVergence bankruptcy proceeding, seeking similar relief.

Irwin Business Finance was also named as a defendant, along with other lenders, in *Sterling Asset & Equity Corp. et al. v. Preferred Capital, Inc. et al.*, an action filed in the United States District Court for the Southern District of Florida in October 2004, which was voluntarily dismissed in January 2005. The plaintiffs then filed a similar complaint in the Circuit Court of the 11th Judicial Circuit, Miami-Dade County, Florida

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on January 14, 2005 seeking class certification on behalf of Florida persons or entities who leased equipment from NorVergence and whose agreement was assigned to one of the named lenders. The plaintiffs allege that NorVergence engaged in false, misleading and deceptive sales and billing practices. The complaint alleges violations of the Florida Deceptive and Unfair Trade Practices Act, the FTC Holder Rule, and breach of contract and warranties. Plaintiffs seek, among other relief, compensatory and punitive damages, injunctive and/or declaratory relief prohibiting enforcement of the leases, rescission, return of payments, interest, attorneys fees and costs.

In addition, Irwin Business Finance has been named in several individual lawsuits involving equipment and services leased from NorVergence, where the lease was assigned to Irwin Business Finance. The suits allege fraud and nonfunctional equipment and services. The plaintiffs request rescission, restitution and/or reformation of the leases and/or a declaration of unenforceability. These suits were filed in the following jurisdictions: two actions in the District Court of Dallas County, Texas (July 2004 and October 2004); one action in the Superior Court of California, County of San Diego (August 2004); and one in the Superior Court of Massachusetts (September 2004). All but the Massachusetts action have been resolved by agreements under which the lessees have paid a significant portion of their lease obligations.

In connection with investigations by various state attorneys general, Irwin Business Finance and other lenders were asked to produce information about their relationships with NorVergence and to refrain from enforcing NorVergence leases. On October 21, 2004, the Attorney General of Florida filed a complaint against twelve lenders, including Irwin Business Finance, in the Circuit Court of the Second Judicial Circuit, Leon County, Florida *(State of Florida v. Commerce Commercial Leasing, LLC et al.).* The complaint alleges that the agreements assigned by NorVergence to the lenders are unconscionable under the Florida Deceptive and Unfair Trade Practices Act. The suit seeks to prohibit collection activities by the lenders and asks for repayment of revenues, rescission of the agreements, restitution, recovery of actual damages, and civil money penalties. Prosecution of this suit against Irwin Business Finance has been stayed by agreement of the parties while they discuss resolution of the concerns expressed by the Florida Attorney General.

Irwin Business Finance was among a number of lenders to receive a notice of intent to sue from the Attorney General of New York. In January 2005, Irwin Business Finance reached an agreement with the New York Attorney General in connection with the five NorVergence-related leases Irwin Business Finance has with New York lessees. The agreement calls for, among other provisions, forgiveness of 90% of the remaining principal balance due on the leases as of July 15, 2004 (approximately $116,000). Irwin Business Finance is also communicating with other state attorneys general about ways in which Irwin Business Finance might work with the states to bring some relief to those who have suffered as a result of the failure of NorVergence.

We are unable to form a reasonable estimate of potential loss, if any, that Irwin Business Finance could suffer as a result of ongoing litigation. Agreements with the various state attorneys general, if reached, would tend to decrease damages awarded, if any, in NorVergence-related class actions and other lawsuits because lessees who accept such agreements would normally cease to be among potential class action plaintiffs. We have not established reserves in connection with NorVergence-related litigation.

We and our subsidiaries are from time to time engaged in various matters of litigation, including the matters described above, other assertions of improper or fraudulent loan practices or lending violations, and other matters, and we have a number of unresolved claims pending. In addition, as part of the ordinary course of business, we and our subsidiaries are parties to litigation involving claims to the ownership of funds in particular accounts, the collection of delinquent accounts, challenges to security interests in collateral, and foreclosure interests, that is incidental to our regular business activities. While the ultimate liability with respect to these other litigation matters and claims cannot be determined at this time, we believe that damages, if any, and other amounts relating to pending matters are not likely to be material to our consolidated financial position or results of operations, except as described above. Reserves are established for these various matters of litigation, when appropriate under SFAS 5, based in part upon the advice of legal counsel.

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Item 4. ***Submission of Matters to a Vote of Security Holders***

During the fourth quarter of 2004, no matters were submitted to a vote of our security holders, through the solicitation of proxies or otherwise.

PART II

Item 5. ***Market for Corporation s Common Equity and Related Stockholder Matters***

Our stock is listed on the New York Stock Exchange under the symbol IFC. The following table sets forth certain information regarding trading in, and cash dividends paid with respect to, the shares of our common stock in each quarter of the two most recent calendar years. The approximate number of shareholders of record on February 18, 2005, was 1,755.

Stock Prices and Dividends:

	Price Range		Quarter	Cash	Total Dividends
	High	**Low**	**End**	**Dividends**	**For Year**
2003					
First quarter	20.12	15.95	19.49	$0.07	
Second quarter	26.50	19.26	25.90	$0.07	
Third Quarter	25.81	20.90	24.30	$0.07	
Fourth Quarter	32.15	25.30	31.40	$0.07	$0.28
2004					
First quarter	36.17	26.63	26.98	$0.08	
Second quarter	27.43	23.10	26.40	$0.08	
Third Quarter	27.58	25.05	25.82	$0.08	
Fourth Quarter	28.85	23.80	28.39	$0.08	$0.32

We expect to continue our policy of paying regular cash dividends, although there is no assurance as to future dividends because they are dependent on future earnings, capital requirements, and financial condition. On February 10, 2005, our Board of Directors approved an increase in the first quarter dividend to $0.10 per share, payable in March 2005. Dividends paid by Irwin Union Bank and Trust and Irwin Union Bank, F.S.B. to the Corporation are restricted by banking law.

Sales of Unregistered Securities:

In 2004, we issued 5,955 shares of common stock pursuant to elections made by eight of our outside directors to receive board compensation under the 1999 Outside Director Restricted Stock Compensation Plan in lieu of cash fees. All of these shares were issued in reliance on the private placement exemption from registration provided in Section 4(2) of the Securities Act.

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Item 6. ***Selected Financial Data***

Five-Year Selected Financial Data

	At or For Year Ended December 31,				
	2004	**2003**	**2002**	**2001**	**2000**
	(Dollars in thousands except per share data)				
For the year:					
Net revenues	$ 524,933	$ 530,445	$ 403,788	$ 387,019	$ 290,626
Noninterest expense	407,235	412,043	317,557	312,819	231,095
Income before income taxes	117,698	118,402	86,231	74,200	59,531
Provision for income taxes	47,794	45,585	33,398	28,859	23,865
Income before cumulative effect of change in accounting principle	69,904	72,817	52,833	45,341	35,666
Cumulative effect of change in accounting principle, net of tax			495	175	
Net income	$ 69,904	$ 72,817	$ 53,328	$ 45,516	$ 35,666
Mortgage loan originations	$13,093,082	$22,669,246	$11,411,875	$ 9,225,991	$4,091,573
Home equity loan originations	1,442,314	1,133,316	1,067,227	1,149,410	1,225,955
Common Share Data:					
Earnings per share:[1]					
Basic	$ 2.47	$ 2.61	$ 1.99	$ 2.15	$ 1.70
Diluted	2.32	2.45	1.89	2.00	1.67
Cash dividends per share	0.32	0.28	0.27	0.26	0.24
Book value per share	17.67	15.36	12.98	10.81	8.92
Dividend payout ratio	12.97%	10.76%	14.01%	12.13%	14.13%
Weighted average shares basic	28,274	27,915	26,823	21,175	20,973
Weighted average shares diluted	31,278	30,850	29,675	24,173	21,593
Shares outstanding end of period	28,452	28,134	27,771	21,305	21,026
At year end:					
Assets	$ 5,239,341	$ 4,988,359	$ 4,910,392	$ 3,446,602	$2,425,690
Residual interests	56,101	71,491	157,514	199,071	152,614
Loans held for sale	890,711	883,895	1,314,849	502,086	579,788
Loans and leases	3,450,440	3,161,054	2,815,276	2,137,822	1,234,922
Allowance for loan and lease losses	44,443	64,285	50,936	22,283	13,129
Servicing assets	367,032	380,123	174,935	228,624	130,627
Deposits	3,395,263	2,899,662	2,693,810	2,308,962	1,442,589

Short-term borrowings	237,277	429,758	993,124	487,963	476,928
Collateralized debt	547,477	590,131	391,425		
Other long-term debt[2]	270,172	270,184	30,070	30,000	30,000
Trust preferred securities[2]			233,000	198,500	153,500
Shareholders equity	502,644	432,260	360,555	231,665	188,870
Managed mortgage banking servicing portfolio	26,196,627	29,640,122	16,792,669	12,875,532	9,196,513
Selected Financial Data:					
Performance Ratios:					
Return on average assets	1.3%	1.4%	1.3%	1.5%	1.8%
Return on average equity	14.8	18.4	16.7	21.8	20.8
Net interest margin[3]	5.46	5.82	6.01	5.35	5.36

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	At or For Year Ended December 31,				
	2004	**2003**	**2002**	**2001**	**2000**
	(Dollars in thousands except per share data)				
Noninterest income to revenues[4]	53.2	53.0	52.3	64.8	69.9
Efficiency ratio[5]	75.7	71.3	70.9	78.1	78.6
Loans and leases and loans held for sale to deposits[6]	91.4	94.1	89.9	79.1	85.6
Average interest-earning assets to average interest-bearing liabilities	132.4	132.2	121.7	117.2	113.5
Asset Quality Ratios:					
Allowance for loan and lease losses to:					
Total loans and leases	1.3%	2.0%	1.8%	1.0%	1.1%
Non-performing loans and leases	131.9	144.9	163.6	116.3	181.8
Net charge-offs to average loans and leases	0.7	1.1	0.7	0.7	0.3
Non-performing assets to total assets	0.9	1.1	0.8	0.7	0.4
Non-performing assets to total loans and leases and other real estate owned	1.3	1.7	1.3	1.1	0.8
Ratio of Earnings to Fixed Charges:					
Including deposit interest	2.3x	2.2x	1.9x	1.6x	1.6x
Excluding deposit interest	3.5	3.1	3.0	2.5	2.5
Capital Ratios:					
Average shareholders equity to average assets	9.0%	7.6%	8.0%	6.7%	8.5%
Tier 1 capital ratio	13.0	11.4	9.3	6.8	8.9
Tier 1 leverage ratio	11.6	11.2	9.7	9.4	12.4
Total risk-based capital ratio	15.9	15.1	13.2	10.8	13.6

(1) Earnings per share of common stock before cumulative effect of change in accounting principle related to SFAS 142, Goodwill and Other Intangible Assets, for the year ended December 31, 2002 was $1.97 basic and $1.87 diluted. Earnings per share of common stock before cumulative effect of change in accounting principle related to SFAS 133, Accounting for Derivative Instruments and Hedging Activities, for the year ended December 31, 2001 was $2.14 basic and $1.99 diluted.

(2) At December 31, 2004 and 2003, the Trusts holding trust preferred securities were not consolidated in accordance with FASB Interpretation No. 46, Consolidation of Variable Interest Entities. See Collateralized and Other Long-Term Debt and footnote 1 to the consolidated financial statements for further discussion.

(3) Net interest income divided by average interest-earning assets.

(4) Revenues consist of net interest income plus noninterest income.

(5) Noninterest expense divided by net interest income plus noninterest income.

(6) Excludes first (but not second) mortgage loans held for sale and loans collateralizing secured financings.

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Item 7. ***Management s Discussion and Analysis of Financial Condition and Results of Operations***
About Forward-looking Statements

You should read the following discussion in conjunction with our consolidated financial statements, footnotes, and tables. This discussion and other sections of this report contain 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. We intend such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995 and are including this statement for purposes of invoking these safe harbor provisions.

Forward-looking statements are based on management s expectations, estimates, projections, and assumptions. These statements involve inherent risks and uncertainties that are difficult to predict and are not guarantees of future performance. In addition, our past results of operations do not necessarily indicate our future results. Words that convey our beliefs, expectations, assumptions, estimates, forecasts, outlook and projections or similar language, or that indicate events we believe could, would, should, may or will occur (or might not occur) or are likely (or unlikely) to occur, and similar expressions, are intended to identify forward-looking statements. These may include, among other things, statements and assumptions about:

- our projected revenues, earnings or earnings per share, as well as management s short-term and long-term performance goals;
- projected trends or potential changes in our asset quality, loan delinquencies, asset valuations, capital ratios or financial performance measures;
- our plans and strategies, including the expected results or impact of implementing such plans and strategies;
- potential litigation developments and the anticipated impact of potential outcomes of pending legal matters;
- the anticipated effects on results of operations or financial condition from recent developments or events;
- any other projections or expressions that are not historical facts.

Actual future results may differ materially from what is projected due to a variety of factors, including, but not limited to:

- potential changes in and volatility of interest rates, which may affect consumer demand for our products and the management and success of our interest rate risk management strategies;
- staffing fluctuations in response to product demand;
- the relative profitability of our lending operations;
- the valuation and management of our servicing portfolios, including short-term swings in valuation of such portfolios due to quarter-end secondary market interest rates, which are inherently volatile;
- borrowers refinancing opportunities, which may affect the prepayment assumptions used in our valuation estimates and which may affect loan demand;
- unanticipated deterioration in the credit quality of our assets;
- deterioration in the carrying value of our other assets, including securities;
- difficulties in delivering products to the secondary market as planned;
- difficulties in expanding our businesses or raising capital and other funding sources as needed;
- competition from other financial service providers for experienced managers as well as for customers;
- changes in the value of companies in which we invest;
- changes in variable compensation plans related to the performance and valuation of lines of business where we tie compensation systems to line-of-business performance;
- unanticipated outcomes in litigation;
- legislative or regulatory changes, including changes in tax laws or regulations, changes in the interpretation of regulatory capital rules, changes in consumer or commercial lending rules or rules affecting corporate governance, and the availability of resources to address these rules;
- changes in applicable accounting policies or principles or their application to our business;
- or governmental changes in monetary or fiscal policies.

We undertake no obligation to update publicly any of these statements in light of future events, except as required in subsequent periodic reports we file with the Securities and Exchange Commission (SEC).

Strategy

Our strategy is to maintain a diverse and balanced revenue stream by focusing on niches in financial services where we believe we can optimize the productivity of our capital and where our experience and expertise can provide a competitive advantage. Our operational objectives are premised on simultaneously achieving three goals: creditworthiness, profitability and growth. We believe we must continually balance these goals in order to deliver long-term value to all of our stakeholders. We have developed a four-part strategy to meet these goals:

Identify underserved niches. We focus on product or market *niches in financial services* that we believe are *underserved* and where we believe customers are willing to pay a premium for value-added services. We don t believe it is necessary to be the largest or leading market share company in any of our product lines, but we do believe it is important that we are viewed as a preferred provider in niche segments of those product offerings.

Hire exceptional management with niche expertise. We enter niches only when we have attracted *senior managers* who have proven track records in the niche for which they are responsible. Each of our five lines of business has a separate management team that operates as an independent business unit responsible for performance goals specific to that particular line of business. Our structure allows the senior managers of each line of business to focus their efforts on understanding their customers and meeting the needs of the markets they serve. This structure also promotes accountability among managers of each enterprise. The senior managers at each of our lines of business and at the parent company have significant industry experience. We attempt to create a mix of short-term and long-term incentives (including, in some instances, minority interests in the line of business) that provide these managers with the incentive to achieve *creditworthy, profitable growth* over the long term.

Diversify capital and earnings risk. We *diversify* our *revenues* and allocate our *capital* across complementary lines of business as a key part of our risk management. Our lines of business are cyclical, but when combined in an appropriate mix, we believe they provide sources of diversification and opportunities for growth in a variety of economic conditions. For example, both the origination and servicing of residential mortgage loans are very cyclical businesses, which normally respond in opposite ways to changes in interest rates and show generally opposite effects in certain economic environments. We believe our participation in these markets has been profitable over time due to our dedication to participating in both segments of the mortgage banking business, rather than one or the other.

Reinvest in new opportunities. We *reinvest* on an ongoing basis in the development of new and existing opportunities. As a result of our attention to long-term value creation, we believe it is important at times to dampen short-term earnings growth by investing for future return. We are biased toward seeking new growth through organic expansion of existing lines of business. At times we will initiate a new line through a start-up, with highly qualified managers we select to focus on a single line of business. Over the past ten years, we have made only a few acquisitions. Those have typically not been in competitive bidding situations.

We believe our historical growth and profitability is the result of our endeavors to pursue complementary consumer and commercial lending niches through our bank holding company structure, our experienced management, our diverse product and geographic markets, and our willingness and ability to align the compensation structure of each of our lines of business with the interests of our stakeholders. Through various economic environments and cycles, we have had a relatively stable revenue and earnings stream on a consolidated basis generated primarily through internal growth rather than acquisitions.

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Critical Accounting Policies/ Management Judgments and Accounting Estimates

Accounting estimates are an integral part of our financial statements and are based upon our current judgments. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ from our current judgments or that our use of different assumptions could result in materially different estimates. The following is a description of the critical accounting policies we apply to material financial statement items, all of which require the use of accounting estimates and/or judgment:

Valuation of Mortgage Servicing Rights

Mortgage servicing rights are recorded at the lower of their allocated cost basis or fair value and a valuation allowance is recorded for any stratum that is impaired. We estimate the fair value of the servicing assets each month using a cash flow model to project future expected cash flows based upon a set of valuation assumptions we believe market participants would use for similar assets. The primary assumptions we use for valuing our mortgage servicing assets include prepayment speeds, default rates, cost to service and discount rates. We review these assumptions on a regular basis to ensure that they remain consistent with current market conditions. Additionally, we periodically receive third party estimates of the portfolio value from independent valuation firms. Inaccurate assumptions in valuing mortgage servicing rights could result in additional impairment and inappropriate hedging decisions and could adversely affect our results of operations. We also review mortgage servicing rights for other-than-temporary impairment each quarter and recognize a direct write-down when the recoverability of a recorded valuation allowance is determined to be remote. Unlike a valuation allowance, a direct write-down permanently reduces the unamortized cost of the mortgage servicing rights asset and the valuation allowance, precluding subsequent reversals. See footnote 7 to the consolidated financial statements for further discussion.

Allowance for Loan and Lease Losses

The allowance for loan and lease losses (ALLL) reflects our estimate of the adequacy of reserves needed to cover probable loan and lease losses and certain risks inherent in our loan portfolio. The ALLL is an estimate based on our judgment applying the principles of SFAS 5, Accounting for Contingencies, SFAS 114, Accounting by Creditors for Impairment of a Loan, and SFAS 118, Accounting by Creditors for Impairment of a Loan Income Recognition and Disclosures. In determining a proper level of loss reserves, management evaluates the adequacy of the allowance on a quarterly basis based on our past loan loss experience, known and inherent risks in the loan portfolio, levels of delinquencies, adverse situations that may affect a borrower s ability to repay, trends in volume and terms of loans and leases, estimated value of any underlying collateral, changes in underwriting standards, changes in credit concentrations, and current economic and industry conditions.

Within the allowance, there are specific and expected loss components. The specific loss component is assessed for loans we believe to be impaired under SFAS 114. We have defined impairment as nonaccrual loans. For loans determined to be impaired, we measure the level of impairment by comparing the loan s carrying value to fair value using one of the following fair value measurement techniques: present value of expected future cash flows, observable market price, or fair value of the associated collateral. An allowance is established when the fair value implies a value that is lower than the carrying value. In addition to establishing allowance levels for specifically identified impaired loans, management determines an allowance for all other loans in the portfolio for which historical experience and/or expected performance indicates that certain losses will occur. These loans are segregated by major product type, and in some instances, by aging, with an estimated loss ratio applied against each product type and aging category. The loss ratio is generally based upon historic loss experience for each loan type as adjusted for certain environmental factors management believes to be relevant. Loans and leases that are determined by management to be uncollectible are charged against the allowance. The allowance is increased by provisions against income and recoveries of loans and leases previously charged off. See the Credit Risk section of Management s Discussion and Analysis and footnote 6 to the consolidated financial statements for further discussion.

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In addition to the ALLL, at our mortgage banking segment we record a reserve for potential losses resulting from origination errors. Such errors include inaccurate appraisals, errors in underwriting, and ineligibility for inclusion in loan programs of government-sponsored entities which relieve us of future credit losses. In determining reserve levels for origination errors, we estimate the number of loans with such errors, the year in which the loss will occur, and the severity of the loss upon occurrence applied to an average loan amount. Inaccurate assumptions in setting this reserve could result in changes in future reserves.

Valuation of Residual Interests

Residual interests from securitizations treated as sales under SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, are classified as trading assets and as such, we record them at fair value on the balance sheet. We record the changes in fair value of these residuals as trading gains or losses in our statement of income in the period of change. We use a discounted cash flow analysis to determine the fair value of these residuals. Cash flows are projected over the lives of the residuals using prepayment, default, and interest rate assumptions that we believe market participants would use for similar financial instruments. Inaccurate assumptions in valuing residual interests could result in additional impairment and adversely affect our results of operations. We have not created these types of residuals since early 2002. See footnote 3 to the consolidated financial statements for further discussion.

Accounting for Deferred Taxes

Deferred tax assets and liabilities are determined based on temporary differences between the time income or expense items are recognized for book purposes and in our tax return. We make this measurement using the enacted tax rates and laws that are expected to be in effect when the differences are expected to reverse. We recognize deferred tax assets based on estimates of future taxable income. Events may occur in the future that could cause the realizability of these deferred tax assets to be in doubt, requiring the need for a valuation allowance.

Consolidated Overview

	2004	% Change	2003	% Change	2002
Net income (millions)	$69.9	(4.0)%	$72.8	36.5%	$53.3
Basic earnings per share[1]	2.47	(5.4)	2.61	31.2	1.99
Diluted earnings per share[1]	2.32	(5.3)	2.45	29.6	1.89
Return on average equity	14.8%		18.4%		16.7%
Return on average assets	1.3		1.4		1.3

(1) Earnings per share of common stock before cumulative effect of change in accounting principle related to SFAS 142, Goodwill and Other Intangible Assets, for the year ended December 31, 2002 was $1.97 basic and $1.87 diluted.

Consolidated Income Statement Analysis

Net Income

We recorded net income of $69.9 million for the year ended December 31, 2004, down 4% from net income of $72.8 million for the year ended December 31, 2003, and compared to $53.3 million in 2002. Net income per share (diluted) was $2.32 for the year ended December 31, 2004, down 5% from $2.45 per share in 2003 and up 23% from $1.89 per share in 2002. Return on equity was 14.8% for the year ended December 31, 2004, 18.4% in 2003 and 16.7% in 2002. The effective income tax rate for 2004 was 40.6%, compared to 38.5% in 2003 and 38.7% in 2002. The higher effective rate in 2004 was caused, in part, by non-deductible interest at our Canadian leasing subsidiary. We believe the effective rate in 2005 will be closer to the rates in 2002 and 2003, rather than the rate in 2004.

Net Interest Income

Net interest income for the year ended December 31, 2004 totaled $252.1 million, down 7% from 2003 net interest income of $271.9 million and up 18% from 2002. The following table shows our daily average consolidated balance sheet and interest rates at the dates indicated:

	December 31,								
	2004			2003			2002		
	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate
	(Dollars in thousands)								
Assets									
Interest-earning assets:									
Interest-bearing deposits with financial institutions	$ 85,304	$ 794	0.93%	$ 74,216	$ 550	0.74%	$ 25,859	$ 311	1.20%
Federal funds sold	15,340	173	1.13	10,824	118	1.10	12,582	104	0.83
Residual interests	67,544	12,509	18.52	108,351	20,651	19.06	186,947	34,164	18.27
Investment securities(2)	88,254	4,536	5.14	68,602	3,723	5.43	39,923	2,809	7.04
Loans held for sale	1,034,032	80,003	7.74	1,237,963	104,350	8.43	668,522	55,336	8.28
Loans and leases, net of unearned income(1)	3,324,333	246,288	7.41	3,168,776	241,592	7.62	2,620,428	218,718	8.35
Total interest earning assets	$4,614,807	$344,303	7.46%	4,668,732	$370,984	7.95%	3,554,261	$311,442	8.76%
Noninterest-earning assets:									
Cash and due from banks	104,115			103,581			100,259		
Premises and equipment, net	31,219			32,644			34,041		
Other assets	586,668			440,164			354,296		
Less allowance for loan and lease losses	(56,311)			(57,986)			(37,054)		
Total assets	$5,280,498			$5,187,135			$4,005,803		
Liabilities and Shareholders Equity									
Interest-bearing liabilities:									
Money market checking	$ 333,772	$ 4,487	1.34%	$ 169,674	$ 913	0.54%	$ 132,351	$ 664	0.50%
Money market savings	1,071,617	15,127	1.41	866,241	11,085	1.28	648,706	10,253	1.58
Regular savings	60,800	873	1.44	62,756	1,249	1.99	58,204	1,586	2.72
Time deposits	907,736	24,000	2.64	992,954	29,118	2.93	1,027,045	41,858	4.08
Short-term borrowings	307,929	9,583	3.11	595,243	14,889	2.50	600,821	15,003	2.50
Collateralized debt	534,660	15,259	2.85	578,656	15,369	2.66	215,128	5,932	2.76
Other long-term debt	270,178	22,896	8.47	30,060	2,325	7.74	31,985	2,699	8.44
Trust preferred securities distributions(3)			n/a	236,823	24,151	10.20	205,400	19,800	9.64
Total interest-bearing liabilities	$3,486,692	$ 92,225	2.65%	$3,532,407	$ 99,099	2.81%	2,919,640	$ 97,795	3.35%
Noninterest-bearing liabilities:									
Demand deposits	1,006,558			1,042,403			577,409		
Other liabilities	314,478			216,111			188,738		
Shareholders equity	472,770			396,214			320,016		

Total liabilities and shareholders equity	$5,280,498	$5,187,135	$4,005,803
Net interest income	$252,078	$271,885	$213,647
Net interest income to average interest earning assets	5.46%	5.82%	6.01%

(1) For purposes of these computations, nonaccrual loans are included in daily average loan amounts outstanding.

(2) We do not show interest income on a tax equivalent basis because it is immaterial

(3) These securities were re-classified in 2004 to Other long-term debt .

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Net interest margin for the year ended December 31, 2004 was 5.46% compared to 5.82% in 2003 and 6.01% in 2002. The decline in margin in 2004 relates to the lower interest rate environment relative to 2003 that caused yields on variable rate loans to decline at a more rapid pace than underlying funding sources, some of which (e.g., mortgage escrow deposits) have rates close to zero in any interest rate environment and, therefore, cannot reduce in a declining rate environment. In addition, the average balance on the high-yielding residual interests declined 38% in 2004 due primarily to the full year effect in 2004 of unrealized trading losses (reflecting valuation impairment) recorded during the first half of 2003.

The following table sets forth, for the periods indicated, a summary of the changes in interest earned and interest paid resulting from changes in volume and rates for the major components of interest-earning assets and interest-bearing liabilities:

	For the Year Ended December 31,					
	2004 Over 2003			2003 Over 2002		
	Volume	Rate	Total	Volume	Rate	Total
	(Dollars and thousands)					
Interest Income						
Loans and leases	$ 11,860	$ (7,164)	$ 4,696	$ 45,769	$ (22,895)	$ 22,874
Mortgage loans held for sale	(17,189)	(7,158)	(24,347)	47,134	1,880	49,014
Investment securities	1,066	(253)	813	2,018	(1,104)	914
Residual interests	(7,777)	(365)	(8,142)	(14,363)	850	(13,513)
Interest bearing deposits with financial institutions	82	162	244	581	(342)	239
Federal funds sold	50	5	55	(15)	29	14
Total	(11,908)	(14,773)	(26,681)	81,124	(21,582)	59,542
Interest Expense						
Money market checking	883	2,691	3,574	187	62	249
Money market savings	2,628	1,414	4,042	3,438	(2,606)	832
Regular savings	(39)	(337)	(376)	124	(461)	(337)
Time deposits	(2,499)	(2,619)	(5,118)	(1,389)	(11,351)	(12,740)
Short-term borrowings	(7,187)	1,881	(5,306)	(139)	25	(114)
Collateralized debt	(1,169)	1,059	(110)	10,024	(587)	9,437
Other long-term debt	18,575	1,996	20,571	(162)	(212)	(374)
Trust preferred securities distribution	(24,151)	0	(24,151)	3,029	1,322	4,351
Total	(12,959)	6,085	(6,874)	15,112	(13,808)	1,304
Net Interest Income	$ 1,051	$ (20,858)	$ (19,807)	$ 66,012	$ (7,774)	$ 58,238

The variance not due solely to rate or volume has been allocated on the basis of the absolute relationship between volume and rate variances.

Provision for Loan and Lease Losses

The consolidated provision for loan and lease losses for the year 2004 was $14.1 million, compared to $47.6 million and $44.0 million in 2003 and 2002, respectively. More information on this subject is contained in the section on credit risk.

Noninterest Income

Noninterest income during the year 2004 totaled $287.0 million, compared to $306.1 million for 2003 and $234.1 million in 2002. The decrease in 2004 versus 2003 was primarily a result of a $180 million or 49%

decrease in gain from sale of loans as a result of decreased production and decreased secondary market deliveries of first mortgage loans. In addition, we recorded impairment on our mortgage servicing asset totaling $2 million in 2004, versus impairment recovery in 2003 of $45 million. Offsetting this was $21 million in derivative gains from our economic hedging activities during 2004, compared to $44 million of derivative losses during 2003. Accordingly, mortgage servicing asset impairment/recovery net of derivative gains/losses was a net recovery of $19 million in 2004 compared to a net recovery of $24 million in 2003. Also offsetting the decreased gain on sale was amortization expense on our servicing asset that decreased 14% to $117 million in 2004 compared to $136 million in 2003 due to lower prepayments and as a result of permanent impairment taken in 2003. These fluctuations in noninterest income primarily occurred at our mortgage banking line of business and relate to market conditions driven by a low interest rate environment throughout most of 2004. See Mortgage Banking section for further discussion. In our Home Equity Lending segment, we recorded trading gains of $25 million in 2004 compared to trading losses of $52 million in 2003. The unrealized gains in 2004 principally reflect lower actual loss rates than those previously modeled and reflect more sizable recoveries resulting from home price appreciation and more aggressive collection efforts. See Home Equity Lending section for further discussion.

Noninterest Expense

Noninterest expenses for the year ended December 31, 2004 totaled $407.2 million, compared to $412.0 million and $317.6 million in 2003 and 2002, respectively. The decrease in consolidated noninterest expense in 2004 is primarily related to lower personnel costs associated with our decreased production at the mortgage banking line of business. This decline was offset by higher personnel costs at the home equity lending, commercial banking, and commercial finance lines of business in connection with their improved performance in 2004.

Consolidated Balance Sheet Analysis

Average assets for 2004 were $5.3 billion up 2% from December 31, 2003, and up 32% from December 31, 2002. The growth in the consolidated average balance sheet reflects increases in portfolio loans and leases particularly at the commercial banking and commercial finance lines of business. This growth was offset by declines in mortgage loans held for sale at the mortgage banking line of business as mortgage production decreased in 2004. Total assets at December 31, 2004 were $5.2 billion, up 5% from December 31, 2003.

Loans Held For Sale

Loans held for sale totaled $0.9 billion at December 31, 2004, unchanged from December 31, 2003 and down 32% from December 31, 2002. The decrease compared to 2002 occurred primarily at our mortgage banking line of business where first mortgage loans held for sale declined from $1.2 billion at December 31, 2002 to $0.7 billion at December 31, 2003 and 2004. This decline reflects slower refinance activity at the mortgage line of business as a result of the interest rate environment at year-end 2003 and 2004. Included in loans held for sale at the mortgage line of business at December 31, 2004 and 2003 were $68 million and $116 million, respectively, of loans for which we have the right, but not the obligation, to repurchase due to default, under the terms of the government servicing agency contracts. Upon default, we have the non-contingent right to repurchase these loans which causes repurchase accounting under Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards (SFAS) No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. The liability associated with these loans is reflected in other liabilities on our Consolidated Balance Sheet.

Loans and Leases

Our commercial loans and leases are originated throughout the United States and Canada. Equipment loans and leases are also originated in Canada by our commercial finance line of business. At December 31, 2004, 93% of our loan and lease portfolio was associated with our U.S. operations. We also extend credit to

consumers nationally through mortgages, installment loans and revolving credit arrangements. Loans by major category for the periods presented were as follows:

	December 31,				
	2004	2003	2002	2001	2000
	(Dollars in thousands)				
Commercial, financial and agricultural	$1,697,651	$1,503,619	$1,347,962	$1,055,307	$ 677,066
Real estate construction	287,496	306,669	314,851	287,228	220,485
Real estate mortgage	808,875	859,541	777,865	490,186	122,301
Consumer	31,166	27,370	27,857	38,489	56,785
Commercial financing:					
Franchise financing	330,496	207,341	130,247	47,447	
Domestic leasing	174,035	157,072	161,464	185,080	116,867
Canadian leasing	265,780	207,355	133,784	91,816	72,864
Unearned income:					
Franchise financing	(86,638)	(56,837)	(34,494)	(11,497)	
Domestic leasing	(23,924)	(22,038)	(24,793)	(32,686)	(21,570)
Canadian leasing	(34,497)	(29,038)	(19,467)	(13,548)	(9,876)
Total	$3,450,440	$3,161,054	$2,815,276	$2,137,822	$1,234,922

The following table shows our contractual maturity distribution of loans at December 31, 2004. Actual principal payments may differ depending on customer prepayments:

	Within One Year	After One But Within Five Years	After Five Years	Total
	(Dollars in thousands)			
Commercial, financial and agricultural	$ 736,322	$ 693,360	$ 267,969	$1,697,651
Real estate construction	192,868	74,690	19,938	287,496
Real estate mortgage	42,137	71,423	695,315	808,875
Consumer	20,715	8,546	1,905	31,166
Commercial financing:				
Franchise financing	10,445	46,611	186,802	243,858
Domestic leasing	10,745	138,129	1,237	150,111
Canadian leasing	11,349	205,401	14,533	231,283
Total	$1,024,581	$1,238,160	$1,187,699	$3,450,440
Loans due after one year with:				
Fixed interest rates				$1,060,852
Variable interest rates				1,365,007
Total				$2,425,859

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Allowance for Loan and Lease Losses

Changes in the allowance for loan and lease losses are summarized below:

	December 31,		
	2004	2003	2002
	(Dollars in thousands)		
Balance at beginning of year	$ 64,285	$ 50,936	$ 22,283
Provision for loan and lease losses	14,195	47,583	43,996
Charge-offs	(28,180)	(37,312)	(18,230)
Recoveries	5,335	3,420	2,870
Reduction due to sale of loans and leases and other	(627)	(234)	
Reduction due to reclassification of loans	(10,808)	(690)	
Foreign currency adjustment	243	582	17
Balance at end of period	$ 44,443	$ 64,285	$ 50,936

The 2004 rollforward of allowance for loan and lease losses above includes the effect of the transfer and sale of portfolio loans at our home equity lending line of business. We transferred $355 million in loans to loans held for sale when the decisions were made to sell these loans from the portfolio. These loans had an associated allowance of $20.6 million. The loans were transferred with an allowance of $10.8 million to reduce their carrying value to fair market value. After the transfers, the remaining $9.8 million of excess allowance was reversed through the provision for loan and lease losses.

Investment Securities

The following table shows the composition of our investment securities at the dates indicated:

	December 31,		
	2004	2003	2002
	(Dollars in thousands)		
U.S. Treasury and government obligations	$ 3,556	$20,994	$14,992
Obligations of states and political subdivisions	3,746	3,960	4,210
Mortgage-backed securities	31,556	2,039	1,738
Other	69,364	65,532	47,008
Total	$108,222	$92,525	$67,948

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Included within the other category is $66 million, $63 million, and $46 million of FHLB and Federal Reserve Bank stock at December 31, 2004, 2003, and 2002, respectively, for which there is no readily determinable market value. The following table shows maturity distribution of our investment securities at December 31, 2004:

	Within One Year	After Five But Within Ten Years	After Ten Years	Mortgage-backed Securities and FHLB & Federal Reserve Bank Stock	Total
			(Dollars in thousands)		
U.S. Treasury and government obligations	$	$	$3,556	$	$ 3,556
Obligations of states and political subdivisions		530	3,216		3,746
Other	3,134				3,134
Total	3,134	530	6,772		10,436
Mortgage-backed securities				31,556	