

IRWIN FINANCIAL CORP

Form 10-K/A

February 03, 2006

**Table of Contents**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, DC 20549  
FORM 10-K/A  
Amendment No. 1**

**(Mark One)**

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

**For the fiscal Year Ended December 31, 2004**

**or**

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

**For the transition period from        to        .  
Commission file number 0-6835**

**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 if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark whether the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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  No

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

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

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

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**

**EXPLANATORY NOTE**

This Report on Form 10-K/A amends the Company's Annual Report on Form 10-K for the period ended December 31, 2004, as initially filed with the Securities and Exchange Commission on March 9, 2005. This restatement, which we announced on November 4, 2005, is a result of our correcting the accounting for incentive servicing fees as mortgage servicing rights rather than derivative instruments. See Note 2 Restatement of Financials for additional information regarding this restatement and a summary of the impact of this restatement on our financial statements. Item 7 - Management's Discussion and Analysis of Financial Condition and Results of Operations has been amended to reflect the impact of the restatement. Item 9A Controls and Procedures has also been amended to acknowledge the existence of a material weakness in our internal controls over financial reporting. In light of the restatement, we have made other adjusting entries to change the period in which the reversal of certain tax reserves were recorded from the first quarter of 2005 to the proper periods in 2004. These tax reserve adjustments were considered immaterial prior to the restatement. The Form 10-K has not been amended in any other respect except for certain minor conforming changes and the provision of updated certifications and signatures.

The financial statements and related financial information for the affected periods contained in our Annual Report on Form 10-K for the period ended December 31, 2004 should no longer be relied upon.

## FORM 10-K/A

**TABLE OF CONTENTS**

<u>Part I</u>		
<u>Item 1</u>	Business	3
<u>Item 2</u>	Properties	14
<u>Item 3</u>	Legal Proceedings	15
<u>Item 4</u>	Submission of Matters to a Vote of Security Holders	19
<u>Part II</u>		
<u>Item 5</u>	Market for Corporation's Common Equity and Related Stockholder Matters	20
<u>Item 6</u>	Selected Financial Data	21
<u>Item 7</u>	Management's Discussion and Analysis of Financial Condition and Results of Operations	22
<u>Item 7A</u>	Quantitative and Qualitative Disclosures about Market Risk	64
<u>Item 8</u>	Financial Statements and Supplementary Data	64
<u>Item 9</u>	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	99
<u>Item 9A</u>	Controls and Procedures	99
<u>Item 9B</u>	Other Information	101
<u>Part III</u>		
<u>Item 10</u>	Directors and Executive Officers of the Corporation	102
<u>Item 11</u>	Executive Compensation	102
<u>Item 12</u>	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	102
<u>Item 13</u>	Certain Relationships and Related Transactions	102
<u>Item 14</u>	Principal Accountant Fees and Services	102
<u>Part IV</u>		
<u>Item 15</u>	Exhibits, Financial Statement Schedules	103
<b>SIGNATURES</b>		106
<u>Computation of Earnings Per Share</u>		
<u>Computation of Earnings to Fixed Charges</u>		
<u>Revised Consent of Registered Public Accounting Firm</u>		
<u>Certification by the CEO</u>		
<u>Certification by the CFO</u>		
<u>Certification of the CEO</u>		

Certification of the CFO

2

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**Table of Contents**

**PART I**

**Item 1. Business  
General**

We are a diversified financial services company headquartered in Columbus, Indiana with \$521.4 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 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.



## **Table of Contents**

### *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.





## **Table of Contents**

### *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.

**Table of Contents**

**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 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 \$164 million qualified as Tier 1 capital as of December 31, 2004); and

minority interests in the common equity accounts of consolidated subsidiaries;

**Table of Contents**

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 \$69 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 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.

**Table of Contents**

*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

**Table of Contents**

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 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.





**Table of Contents**

*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 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

**Table of Contents**

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

**Table of Contents**

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.

## **Table of Contents**

### *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.



**Table of Contents**

*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.

**Table of Contents**

**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.

**Table of Contents***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.

**Table of Contents**

*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 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

**Table of Contents**

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 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 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



**Table of Contents**

suits were filed in the following jurisdic