

IRWIN FINANCIAL CORP

Form 10-K

March 14, 2008

Table of Contents

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549**

FORM 10-K

(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, 2007

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:

Title of Common Stock*

Class:

**Title of 8.70% Cumulative Trust Preferred Securities issued by IFC Capital Trust VI and the
Class: guarantee with respect thereto.**

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

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 if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes No

Edgar Filing: IRWIN FINANCIAL CORP - Form 10-K

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 registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

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, computed by reference to the closing price for the registrant's common stock on the New York Stock Exchange on June 30, 2007, was approximately \$276,290,152.

As of March 7, 2008, there were outstanding 29,600,284 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 May 30, 2008	Part III
Exhibit Index on Pages 119 through 122	

FORM 10-K
TABLE OF CONTENTS

	<u>About Forward-looking Statements</u>	2
<u>Part I</u>		
<u>Item 1</u>	<u>Business</u>	4
<u>Item 1A</u>	<u>Risk Factors</u>	14
<u>Item 1B</u>	<u>Unresolved Staff Comments</u>	19
<u>Item 2</u>	<u>Properties</u>	19
<u>Item 3</u>	<u>Legal Proceedings</u>	20
<u>Item 4</u>	<u>Submission of Matters to a Vote of Security Holders</u>	22
<u>Part II</u>		
<u>Item 5</u>	<u>Market for -Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	23
<u>Item 6</u>	<u>Selected Financial Data</u>	24
<u>Item 7</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	25
<u>Item 7A</u>	<u>Quantitative and Qualitative Disclosures about Market Risk</u>	71
<u>Item 8</u>	<u>Financial Statements and Supplementary Data</u>	71
<u>Item 9</u>	<u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	117
<u>Item 9A</u>	<u>Controls and Procedures</u>	117
<u>Item 9B</u>	<u>Other Information</u>	117
<u>Part III</u>		
<u>Item 10</u>	<u>Directors, Executive Officers, and Corporate Governance</u>	118
<u>Item 11</u>	<u>Executive Compensation</u>	118
<u>Item 12</u>	<u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	118
<u>Item 13</u>	<u>Certain Relationships and Related Transactions, and Director Independence</u>	118
<u>Item 14</u>	<u>Principal Accountant Fees and Services</u>	118
<u>Part IV</u>		
<u>Item 15</u>	<u>Exhibits and Financial Statement Schedules</u>	119
<u>SIGNATURES</u>		123
	<u>Business Development Board Compensation Program</u>	
	<u>Notice of Restricted Stock Unit Award</u>	
	<u>Computation of Earnings Per Share</u>	
	<u>Computation of Ratio of Earnings to Fixed Charges</u>	
	<u>Code of Conduct</u>	
	<u>Subsidiaries</u>	
	<u>Consent of Independent Registered Public Accounting Firm</u>	
	<u>Consent of Independent Registered Public Accounting Firm</u>	
	<u>Certification by the CEO</u>	
	<u>Certification by the CFO</u>	
	<u>Section 906 Certification by the CEO</u>	
	<u>Section 906 Certification by the CFO</u>	

Table of Contents

About Forward-looking Statements

This report contains 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. We 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, views, 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 asset quality (particularly with regard to loans or other exposures including loan repurchase risk, in sectors in which we deal in real estate or residential mortgage lending), loan delinquencies, charge-offs, reserves, asset valuations, capital ratios or financial performance measures;

our plans and strategies, including the expected results or costs and impact of implementing or changing such plans and strategies;

potential litigation developments and the anticipated impact of potential outcomes of pending legal matters;

predictions about conditions in housing markets, industries associated with housing, the mortgage markets or mortgage industry;

the anticipated effects on results of operations or financial condition from recent developments or events; and

any other projections or expressions that are not historical facts.

We qualify any forward-looking statements entirely by these cautionary factors.

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

potential deterioration or effects of general economic conditions, particularly in sectors relating to real estate and/or mortgage lending or small business-based manufacturing and services;

potential effects related to the Corporation's decision to suspend the payment of dividends on its common, preferred and trust preferred securities.

potential changes in direction, volatility and relative movement (basis risk) of interest rates, which may affect consumer and commercial demand for our products and the management and success of our interest rate risk

management strategies;

competition from other financial service providers for experienced managers as well as for customers;

staffing fluctuations in response to product demand or the implementation of corporate strategies that affect our work force and potential associated charges;

the relative profitability of our lending and deposit operations;

the valuation and management of our portfolios, including the use of external and internal modeling assumptions we embed in the valuation of those portfolios and short-term swings in the valuation of such portfolios;

borrowers' refinancing opportunities, which may affect the prepayment assumptions used in our valuation estimates and which may affect loan demand;

Table of Contents

unanticipated deterioration in the credit quality or collectibility of our loan and lease assets, including deterioration resulting from the effects of natural disasters;

difficulties in accurately estimating the future repurchase risk of residential mortgage loans due to alleged violations of representations and warrants we made when selling the loans to the secondary market;

unanticipated deterioration or changes in estimates of the carrying value of our other assets, including securities;

difficulties in delivering products to the secondary market as planned;

difficulties in expanding our businesses and obtaining or retaining deposit or other funding sources as needed;

changes in the value of our lines of business, subsidiaries, or 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 laws, rules or regulations that affect tax, consumer or commercial lending, corporate governance and disclosure requirements, and other laws, rules or regulations affecting the rights and responsibilities of our Corporation, bank or thrift;

regulatory actions that impact our Corporation, bank or thrift, including the memorandum of understanding entered into as of March 1, 2007 between Irwin Union Bank and Trust and the Federal Reserve Bank of Chicago;

changes in the interpretation of regulatory capital or other rules;

the availability of resources to address changes in laws, rules or regulations or to respond to regulatory actions;

changes in applicable accounting policies or principles or their application to our business or final audit adjustments, including additional guidance and interpretation on accounting issues and details of the implementation of new accounting methods;

the final disposition of our remaining assets and obligations of our discontinued mortgage banking segment; 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 reports we file with the Securities and Exchange Commission (SEC).

Table of Contents

PART I

Item 1. *Business*

General

We are a bank holding company headquartered in Columbus, Indiana with \$155 million of net revenues from continuing operations in 2007 and \$6.2 billion in assets at December 31, 2007. We focus primarily on the extension of credit to small businesses and consumers as well as providing the ongoing servicing of those customer accounts. Through our direct and indirect subsidiaries, we currently operate three major lines of business: commercial banking, commercial finance, and home equity lending. In 2006, we sold the majority of our conforming conventional first mortgage banking business.

We conduct our commercial and consumer 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, conducts our commercial banking activities; Irwin Commercial Finance Corporation, a commercial finance subsidiary; and Irwin Home Equity Corporation, a consumer home equity lending company. In 2006, we discontinued the majority of operations at Irwin Mortgage Corporation, our mortgage banking company and formerly one of our major subsidiaries.

Our strategy is to position the Corporation as an interrelated group of specialized financial services companies serving niche markets of small businesses and consumers while optimizing the productivity of our capital. We seek to create competitive advantage within the banking industry by serving small businesses and consumers with lending, leasing, deposit, advisory services and specialized mortgage products. Our strategic objective is to create value through well-controlled, profitable growth by attracting, retaining and developing exceptional management teams at our lines of business and parent company who focus on (i) meeting customer needs rather than simply offering banking products or services, (ii) being cost-efficient in our delivery, and (iii) having strong risk management systems. We believe we must continually balance these three factors in order to deliver long-term value to all of our stakeholders. Our lines of business operate as direct and indirect subsidiaries of Irwin Union Bank and Trust (and, in the case of commercial banking, with Irwin Union Bank, F.S.B.). This structure allows us to offer insured deposits 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). Unless otherwise indicated, 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

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,

Edgar Filing: IRWIN FINANCIAL CORP - Form 10-K

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, each headquartered in Columbus, Indiana:

Irwin Union Bank and Trust Company 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

Table of Contents

well as in Grandville (near Grand Rapids), Kalamazoo, Lansing and Traverse City, Michigan; Carson City and Las Vegas, Nevada; and Salt Lake City, Utah.

Irwin Union Bank, F.S.B. is a full-service federal savings bank that began operations in December 2000. Currently we have offices located in Mesa and Phoenix, Arizona; Costa Mesa and Sacramento, California; Louisville, Kentucky; Clayton (near St. Louis), Missouri; Reno, Nevada; Albuquerque, New Mexico; and Milwaukee, Wisconsin. We opened offices in Ohio and Florida in 2007.

We discuss this line of business further in the Commercial Banking section of Management's Discussion and Analysis of Financial Condition and Results of Operation (MD&A) of this report.

Commercial Finance

Established in 1999, our commercial finance line of business originates small-ticket equipment leases throughout the U.S. and Canada and provides equipment and leasehold improvement financing for franchisees (mainly in the quick service restaurant sector) 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 while limiting the industry and geographic concentrations in our lease and loan portfolios. Loans to franchisees often include the financing of real estate as well as equipment. In 2006, this segment expanded its product line to include professional practice financing and information technology leasing to middle and upper middle market companies throughout the United States and Canada.

We discuss this line of business further in the Commercial Finance 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, headquartered in San Ramon, California. Irwin Home Equity became a subsidiary of Irwin Union Bank and Trust in 2001. The Board of Irwin Union Bank and Trust recently approved the merger of Irwin Home Equity into the Bank. This will not affect our operations, but may result in more favorable tax treatment for the Corporation. In conjunction with Irwin Union Bank and Trust, Irwin Home Equity originates, purchases, securitizes and services first mortgages and home equity loans and lines of credit nationwide. Our target customers are principally creditworthy, homeowners with limited equity in their homes as well as lenders/third parties that can benefit from specialized servicing. We market our first mortgage and home equity offering principally through mortgage brokers and correspondent lenders and also direct to consumers.

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

Discontinuance of Mortgage Banking

We discontinued our mortgage banking line of business with the sale of the majority of the assets of Irwin Mortgage Corporation. We sold the production and most of the headquarters operations of this segment in September 2006. We sold the bulk of our portfolio of mortgage servicing rights to multiple buyers, transferring these assets in early January 2007. We sold our servicing platform in January 2007. Prior to the sales, Irwin Mortgage, a subsidiary of Irwin Union Bank and Trust Company, had engaged in the origination, purchase, sale and servicing of conventional and government agency-backed residential mortgage loans. Irwin Mortgage also engaged in the mortgage reinsurance business through its subsidiary, Irwin Reinsurance Corporation, a Vermont Corporation, which we have retained. Irwin Mortgage no longer originates loans but continues to manage and service loans that were not included in the transfer of assets and to manage residual liabilities and responsibilities from prior activities. This segment is accounted

for as discontinued operations.

Customer Base

No single part of our lending business is dependent upon a single borrower or upon a very few borrowers nor would the loss of any one loan customer automatically have a materially adverse effect upon our business.

Table of Contents

We have a number of funding sources which are important to our operations, some of which are customers of our institutions (e.g., depositors) and for some of which we are customers (e.g., lenders). For example, we are a member (and customer) of the Federal Home Loan Bank of Indianapolis, we have a significant Canadian dollar funding facility with a single bank domiciled in Canada, and we have a significant deposit relationship with one of our commercial banking branches. In those instances where we have significant single relationships, on the funding side of the balance sheet, we examine each relationship more intensively than others and have developed contingency plans for the loss of these significant customer relationships. The loss of any one of these significant relationships would require changes to our funding program.

Competition

We compete nationally in the U.S. in each business, except for commercial banking where our market focus is in selected markets in the Midwest and Western states. In our commercial finance line of business, certain of our equipment leasing products are also offered throughout Canada. We compete against commercial banks, savings banks, credit unions and savings and loan associations, and with a number of non-bank companies including mortgage banks and brokers, insurance companies, securities firms, other finance companies, and real estate investment trusts.

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, cost of funds, operating costs, and market penetration.

Employees and Labor Relations

At January 31, 2008 we and our subsidiaries had a total of 1,256 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.

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 \$18 million in 2007, \$17 million in 2006, and \$12 million in 2005. The remainder of our revenues comes from customers and operations in the United States.

Supervision and Regulation

General

We and our subsidiaries are each extensively regulated under state and federal law. The following is a summary of certain 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 are subject to both state and federal examination on matters 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 and intercompany transactions, the adequacy of the reserve for loan losses, regulatory reporting, adequacy of systems of internal controls and limitations on permissible activities.

In addition, we are required to maintain 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.

Table of Contents

Regulatory agencies have a broad range of sanctions and enforcement powers if an institution fails to meet regulatory requirements, 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 imposes risk-based capital requirements on us as a bank holding company. Under these requirements, capital is classified into two categories:

Tier 1 capital, or core capital, consists of

common stockholders' equity;

qualifying noncumulative perpetual preferred stock;

qualifying cumulative perpetual preferred stock, and subject to some limitations, our Trust Preferred securities; and

minority interests in the common equity accounts of consolidated subsidiaries;

less

Accumulated net gains (losses) on cash flow hedges and increase (decrease) recorded in accumulated other comprehensive income (AOCI) for defined benefit postretirement plans under FAS 158

goodwill;

credit-enhancing interest-only strips (certain amounts only); and

specified intangible assets.

Tier 2 capital, or supplementary capital, consists of

allowance for loan and lease losses;

perpetual preferred stock and related surplus;

hybrid capital instruments including, to the extent not included in Tier 1 Capital, Trust Preferred securities;

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 Tier 1 leverage ratio, which is the ratio of Tier 1 capital to total assets (less goodwill and other specified intangible assets), 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 Tier 1 leverage ratio is 4 percent. The Federal Reserve considers the Tier 1 leverage ratio in evaluating proposals for expansion or new activities.

Table of Contents

As of December 31, 2007, we had regulatory capital in excess of all the Federal Reserve's minimum levels. Our ratio of total capital to risk weighted assets at December 31, 2007 was 12.6% and our Tier 1 leverage ratio was 10.2%.

Expansion

Under the BHC Act, we must obtain prior Federal Reserve approval for certain activities, such as the acquisition of more than 5% of the voting shares of any company, including a bank or bank holding company. The BHC Act permits a bank holding company to 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 discussion of *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.

In consideration of the Corporation's recent losses, on February 28, 2008, the Board of Directors elected to defer dividend payments on the Corporation's trust preferred securities and elected to discontinue payment of dividends on its non-cumulative perpetual preferred and common stock. Mindful of regulatory policy and the current economic environment, the Board took these steps to maintain the capital strength of the Corporation at a time of elevated uncertainty in the economy. The Board believes the elevated uncertainty in the current environment demands a greater bias to capital retention on a precautionary basis than distribution of cash from retained earnings for maintenance of historic dividends. The Board will reassess its dividend policy regularly. The ability to pay future dividends is subject to the regulatory restrictions referenced above and in the discussion in the section on *Dividend Limitations* below.

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. Each of the principal subsidiaries of Irwin Union Bank and Trust are routinely subject to examination.

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

The deposits of Irwin Union Bank and Trust and Irwin Union Bank, F.S.B. are insured by the Deposit Insurance Fund of the Federal Deposit Insurance Corporation (FDIC) to the maximum extent permitted by law, which is currently \$100,000 per depositor for all accounts in the same title and capacity, other than individual retirements accounts, certain eligible deferred compensation plans, and so-called Keogh plans or HR 10 plans, which currently

Table of Contents

are insured up to a maximum of \$250,000 per participant in the aggregate, such maximums in each case to be adjusted for inflation beginning in 2010. As a result, Irwin Union Bank and Trust and Irwin Union Bank, F.S.B. are subject to FDIC supervision and regulation.

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 their activities and financial condition. Also, before establishing branches or entering into certain transactions such as mergers with, or acquisitions of, other financial institutions, Irwin Union Bank and Trust must obtain regulatory approvals from the Indiana Department of Financial Institutions and the Federal Reserve, and Irwin Union Bank, F.S.B. must obtain approval from the OTS.

Capital Requirements

The Federal Reserve imposes requirements on state member banks such as Irwin Union Bank and Trust regarding the maintenance of adequate capital substantially identical 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 banking institutions rated composite 1 under the uniform rating system of banks and not experiencing or anticipating significant growth 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 or risk profiles of individual banks. The standards set forth above specify minimum supervisory ratios based primarily on broad credit risk considerations. Banks, including ours, are generally expected to operate with capital positions above the minimum ratios.

At December 31, 2007, Irwin Union Bank and Trust had a total risk-based capital ratio of 12.5%, compared to our internal Policy minimum of 12%. Irwin Union Bank and Trust had a Tier 1 capital ratio of 10.7%, and a leverage ratio of 10.6%.

The risk-based capital guidelines also provide that an institution's exposure to declines in the economic value of the institution's capital due to changes in interest rates must be considered as a factor by the agencies in evaluating the capital adequacy of a bank or savings association. This assessment of interest rate risk management is incorporated into the bank's 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 Deposit Insurance Fund. As a result of the Federal Deposit

Insurance Reform Act of 2005, the FDIC adopted a revised risk-based assessment system to determine assessment rates to be paid by member institutions such as Irwin Union Bank and Trust and Irwin Union Bank, F.S.B. Under this revised assessment system, risk is defined and measured using an institution's supervisory ratings with certain other risk measures, including certain financial ratios. The annual rates for 2007 for institutions in risk category I range from 5 to 7 basis points; the rate for institutions in risk category II is 10 basis points; and the rate for institutions in risk category III is 28 basis points. These rates may be offset by a one-time assessment credit held by an institution, based on the assessment base of that institution as of December 31, 1996, and in the future by

Table of Contents

dividends that may be declared by the FDIC if the deposit reserve ratio increases above a certain amount. The FDIC may raise or lower these assessment rates based on various factors to achieve a reserve ratio, which the FDIC currently has set at 1.25 percent of insured deposits.

In addition to deposit insurance fund assessments, the FDIC assesses all 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, 2007, the annualized rate established by the FDIC for the FICO assessment was 1.14 basis points (0.00014%) per \$100 of insured deposits.

Dividend Limitations

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 addition, 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. As a result of our losses in 2007, the bank cannot declare a dividend to us without regulatory approval until such time that current year earnings plus earnings from the last two years exceeds dividends during the same periods. We sought and were granted such approval for a \$15 million dividend in the second quarter of 2007. Our ability to pay dividends on our Trust Preferred, non-cumulative perpetual preferred, and common stock is dependent on our ability to dividend from Irwin Union Bank and Trust, for which prior approval would be necessary.

In consideration of the Corporation's recent losses, on February 28, 2008, the Board of Directors elected to defer dividend payments on the Corporation's trust preferred securities and elected to discontinue payment of dividends on its non-cumulative perpetual preferred and common stock. See the discussion above on *Dividends* in the section on *Bank Holding Company Regulation*.

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 prompt corrective action standards described below under *Other Safety and Soundness Regulations*. 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 federal law, banks are permitted, if they are adequately or well-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

Table of Contents

establish or operate a branch in any state outside the state of its home office if the association meets certain 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. 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. Irwin Union Bank and Trust received a satisfactory rating, and Irwin Union Bank, F.S.B. received an outstanding 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 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 savings banks must meet three minimum capital standards: an 8% risk-based capital ratio, a 4% leverage ratio (or 3% for those assigned a composite rating of 1), and a 1.5% tangible capital ratio. 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. Due to its capital ratios, Irwin Union Bank and Trust and Irwin Union Bank, F.S.B. are permitted to, and do, accept brokered deposits.

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

Table of Contents

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

The lending activities of Irwin Union Bank and Trust and its subsidiaries, Irwin Commercial Finance and Irwin Home Equity, are regulated by the Federal Reserve. 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 Commercial Finance and Irwin Home Equity due to their status as subsidiaries of Irwin Union Bank and Trust.

Our subsidiaries also are subject to federal and state consumer protection and fair lending 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. In many instances, these acts 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. Specifically, these acts, among other things:

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 federal and state regulations that offer consumer protections to depositors, including account terms and disclosures, funds availability and electronic funds transfers.

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 state member bank insured by the FDIC, 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, including at a branch located in a state other than the Bank's home state, regardless of any inconsistent state law, and to apply these rates to loans to borrowers in other states. 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. 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.

Irwin Union Bank and Trust entered into a memorandum of understanding with the Federal Reserve Bank of Chicago as of March 1, 2007 to enhance the consumer compliance function and compliance oversight programs of the Bank and its subsidiaries. Under the memorandum of understanding, which is considered an informal

Table of Contents

agreement, Irwin Union Bank and Trust agreed, among other things, to enhance the Bank-wide perspective on consumer compliance oversight and the risk assessment process, undertake an initial and ongoing review of lending policies and procedures, improve the risk monitoring, issues tracking, training and control programs of the Bank, and enhance the resources devoted to this area. In addition, the Bank agreed to and did provide quarterly written progress reports to the Federal Reserve Bank of Chicago with respect to these matters through the required period ending September 30, 2007. We believe we have been responsive in developing and implementing plans to address the issues raised by the Federal Reserve Bank of Chicago. We are waiting for the Federal Reserve Bank of Chicago to perform a validation of the actions we took to address their concerns. However, if the Federal Reserve Bank of Chicago concludes the actions we took are not sufficient, we could experience additional regulatory action.

Proposed Federal and State Laws and Regulations

Currently, there are a number of proposed and recently enacted federal, state and local laws and regulations and guidance, including changes to the Truth in Lending Act and accompanying regulations, addressing mortgage lending, purchasing and servicing practices. Many of these laws and regulations focus on borrowers with blemished credit or nontraditional mortgage products, while others take a broader approach. For example, Congress is considering several bills to combat abuses in the mortgage lending market and to provide substantial new protections to mortgage consumers. While it is not possible to predict which of these bills will pass, key provisions of the bills under consideration would:

establish a federal duty of care owed by mortgage originators to mortgage applicants and borrowers;

prohibit steering of borrowers into subprime loans if they qualify for prime loans;

establish minimum federal standards for licensing or registration of mortgage originators, including brokers and bank loan officers;

establish minimum underwriting standards for all mortgages, including requiring lenders to determine that borrowers have a reasonable ability to repay and that loans provide borrowers a tangible net benefit;

extend limited liability to secondary market securitizers who acquire, package and sell interests in home mortgage loans that do not meet these standards;

establish new loan servicing and appraisal standards, and impose penalties for violations of these standards; and

expand and enhance consumer protections for certain high-cost, sub-prime and non-traditional loans.

Congress and the Treasury Department also are considering various proposals to expand federal housing finance programs to address liquidity concerns and improve consumer access to mortgage credit, as well as to allow consumers to modify the interest rates, loan maturities or principal balances on mortgages secured by a borrower's principal residence.

The Federal Reserve has issued a proposal to modify the regulations governing the Truth in Lending Act that would, among other things, apply the following protections to all loans secured by a consumer's principal dwelling, regardless of the loan's Annual Percentage Rate: (1) lenders would be prohibited from making payments, directly or indirectly, to mortgage brokers, including through yield-spread premiums, unless the broker previously entered into a written agreement with the consumer disclosing the broker's total compensation and other facts; (2) creditors and mortgage brokers would be prohibited from coercing a real estate appraiser to misstate a home's value; and (3) companies that

service mortgage loans would be prohibited from engaging in certain practices. While the final form of the rules cannot be predicted, it is expected the Fed will issue a final regulation by mid-2008.

Executive Officers

Our executive officers are elected annually by the Board of Directors and serve until their successors are qualified and elected. In addition to our Chief Executive Officer, Chairman and President, Mr. William I. Miller (51), who also serves as a director, our executive officers are listed below as of January 31, 2008.

Table of Contents

Gregory F. Ehlinger (45) has been our Chief Financial Officer since August of 1999. He was a Senior Vice President from August 1999 to February 5, 2008. He has been one of our officers since August 1992.

Bradley J. Kime (47) has been President of our Commercial Banking line of business since May 2003 and President of Irwin Union Bank F.S.B. since December 2000. He has served in several executive officer positions since joining Irwin in 1986.

Joseph R. LaLeggia (46) has been President of our Commercial Finance line of business since July of 2002. He has served in executive officer positions since joining Irwin in 2000.

Jocelyn Martin-Leano (46) has served as President of our Home Equity line of business since July 1, 2006, having been Interim President for the six months prior to that. She has served in executive officer positions since joining Irwin in 1995.

Matthew F. Souza (51) was named Chief Administrative Officer as of February 5, 2008. He was our Senior Vice President-Ethics from August 1999 to February 5, 2008, and has been our Secretary and an officer since 1986.

Item 1A. Risk Factors

An investment in our securities involves a number of risks. We urge you to read all of the information contained in this Report on Form 10-K. In addition, we urge you to consider carefully the following factors in evaluating an investment in our common shares.

Risks Relating to General Economic Conditions and Interest Rates.

We may be adversely affected by a general deterioration in economic conditions.

The risks associated with our business become more acute in periods of a slowing economy or slow growth such as we experienced in the latter half of 2007 and which has continued so far into 2008. Economic declines may be accompanied by a decrease in demand for consumer and commercial credit and declining real estate and other asset values. The credit quality of commercial loans and leases where the activities of the borrower or vendor are related to housing and other real estate markets may decline in periods of stress in these industries. Delinquencies, foreclosures and losses generally increase during economic slowdowns or periods of slow growth. We expect that our servicing costs and credit losses will increase during periods of economic slowdown or slow growth such as the one we are presently experiencing.

In our home equity line of business, a material decline in real estate values may reduce the ability of borrowers to use home equity to support borrowings and could increase the loan-to-value ratios of loans we have previously made, thereby weakening collateral coverage and increasing the possibility of a loss in the event of a default. A decline in real estate values could also materially reduce the amount of home equity loans we produce and lower runoff in our existing portfolio, effectively extending the average life of the loans in the portfolio (and therefore prolonging the period we are exposed to losses).

We may be adversely affected by interest rate changes.

We and our subsidiaries are subject to interest rate risk. Changes in interest rates will affect the value of loans, deposits and other interest-sensitive assets and liabilities on our balance sheet. Our income may be at risk because changes in interest rates also affect our net interest margin and the value of assets and derivatives that we sell from time to time or that are subject to either mark-to-market accounting or lower-of-cost-or-market accounting, such as

loans held for sale, mortgage servicing rights and derivatives instruments.

Reductions in interest rates expose us to write-downs in the carrying value of the mortgage servicing and other servicing assets we hold on our balance sheet. These assets are recorded at the lower of their cost or market value and a valuation allowance is recorded for any impairment. Decreasing interest rates often lead to increased prepayments in the underlying loans, which requires that we write down the carrying value of these servicing assets. The change in value of these assets, if improperly hedged or mismanaged, could adversely affect our operating results in the period in which the impairment occurs.

Table of Contents

Our lines of business mainly depend on earnings derived from net interest income. Net interest income is the difference between interest earned on loans and investments and the interest expense paid on other borrowings, including deposits at our banks and other funding liabilities we have. Our interest income and interest expense are affected by general economic conditions and by the policies of regulatory authorities, including the monetary policies of the Federal Reserve that cause our funding costs and yields on new or variable rate assets to change.

Although we take measures intended to manage the risks of operating in changing interest rate environments, we cannot eliminate interest rate sensitivity. Our goal is to ensure that interest rate sensitivity does not exceed prudent levels as determined by our Board of Directors in certain policies. Our risk management techniques include modeling interest rate scenarios, using financial hedging instruments, and match-funding certain loan assets. There are costs and risks associated with our risk management techniques, and these could be substantial.

Finally, to reduce the effect interest rates have on our businesses, we periodically invest in derivatives and other interest-sensitive instruments. While our intent in purchasing these instruments is to reduce our overall interest rate sensitivity, the performance of these instruments can, at times, cause volatility in our results either due to factors such as basis risk between the derivatives and the hedged item, timing of accounting recognition differences or other such factors.

Risks Relating to an Investment in Us.

We have recently had financial performance below that of peers and have lost money in each of the past four quarters.

In 2007 and the first and third quarters of 2006, we lost money, due in large part to the sale of our conforming mortgage banking segment and conditions in the residential mortgage and real estate industries.

While our current projections indicate that we will return to profitability in 2008, the uncertainty of all forecasts has increased substantially.

The unexpected losses sustained by the Corporation in the third and fourth quarters of 2007 can be directly traced to the unprecedented dislocation in the housing markets, rising unemployment, and less liquidity in certain portions of the credit markets.

The size of the third quarter loss in 2007 was primarily driven by the adjustment to the repurchase reserve in discontinued operations, reflecting a spike in repurchase demands in the third quarter. While we believe that the risk of needing additional reserves is declining as time passes (additional reserves were not required in the fourth quarter), this repurchase risk remains.

The size of the loss in the fourth quarter of 2007 was primarily driven by the acceleration of delinquencies at home equity in that quarter. The allowance for loan losses in this segment at the end of the fourth quarter was established assuming this negative trend continues into 2008.

While we believe we are addressing the factors that caused this underperformance, there can be no assurance if and when our results will surpass that of our peers.

We may need additional capital in the future and adequate financing may not be available to us on acceptable terms, or at all.

While we anticipate that we would be able to access capital markets as necessary to fund the growth of our business, the uncertainty of continued access increased due to market conditions in 2007. Our current capital levels exceed our internal policies. However, in consideration of the Corporation's recent losses, on February 28, 2008, the Board of Directors elected to curtail additional corporate borrowings at the parent company level, with certain exceptions, in an aggregate amount greater than the indebtedness currently outstanding until such time as the Board determines that economic conditions and our profitability have improved. The restriction on additional borrowings does not apply to our subsidiaries Irwin Union Bank and Trust Company or Irwin Union Bank, FSB. If we were to seek additional capital in the future to fund growth of our operations or to maintain our regulatory capital above well-capitalized standards, there is no assurance we would be able to obtain additional debt or equity financing, or, if available, it will be obtainable in amounts and on terms attractive or acceptable to us. If we choose to raise equity

Table of Contents

capital on unattractive terms, it could be highly dilutive to current shareholders. If we are unable to obtain the funding we need, we may be unable to develop our products and services, take advantage of future opportunities or respond to competitive pressures, which could have a material adverse effect on us.

Our operations may be adversely affected if we are unable to secure adequate funding; our use of wholesale funding sources and securitizations exposes us to potential liquidity risk.

Our discontinued mortgage banking line of business was a net provider of liquidity to the Corporation. Our divestiture of this segment has caused us to seek alternative funding sources to contribute to our other lines of business, which sources might be more expensive than those previously used.

Due to the sale of mortgage servicing rights and the loss of escrow deposits associated with those servicing rights, we have increased our reliance on wholesale funding, such as Federal Home Loan Bank borrowings and brokered deposits in recent quarters. Because wholesale funding sources are affected by general capital market conditions, the availability of funding from wholesale lenders may be dependent on the confidence these investors have in commercial and consumer finance businesses. We also have a significant deposit relationship with one of our commercial banking branches. While we have processes in place to monitor and mitigate these funding risks, the continued availability to us of these funding sources is uncertain, and we could be adversely impacted if our business segments become disfavored by wholesale lenders or large depositors. In addition, brokered deposits may be difficult for us to retain or replace at attractive rates as they mature. Our financial flexibility could be severely constrained if we are unable to renew our wholesale funding or if adequate financing is not available in the future at acceptable rates of interest. We may not have sufficient liquidity to continue to fund new loans or lease originations and we may need to liquidate loans or other assets unexpectedly in order to repay obligations as they mature.

Historically, we have financed or sold the majority of our second mortgage loan originations into the secondary market through the use of securitizations. This market closed to all participants in the middle of 2007. We expect it to remain closed indefinitely. In addition, certain of our high loan-to-value home equity loans are not readily marketable, and we may not be able to sell assets at favorable prices when necessary. This could adversely affect our profitability and/or liquidity for future originations and purchases of loans.

We have regulatory restrictions on our ability to receive dividends from bank subsidiaries.

Irwin Union Bank and Trust may not, without the approval of the Federal Reserve and the Indiana Department of Financial Institutions, 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. During the past two years, Irwin Union Bank and Trust dividends have exceeded net income during the same period. As a result, the bank cannot declare a dividend to us without regulatory approval until such time that current year earnings plus earnings from the last two years exceeds dividends during the same periods. We last sought and were granted such approval for a \$15 million dividend in the second quarter of 2007, but similar responses to future requests are not guaranteed. We are mindful that the Federal Reserve has publicly expressed the belief 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. Our Board of Directors has therefore elected to defer dividend payments on the Corporation's trust preferred securities and elected to discontinue payment of dividends on its non-cumulative perpetual preferred and common stock. Our ability to pay dividends in the future depends on our ability to dividend from Irwin Union Bank and Trust to the Corporation, for which prior approval from our regulators and additional action by our Board of Directors will be necessary.

We have credit risk inherent in our asset portfolios.

In our businesses, some borrowers may not repay loans that we make to them. As all financial institutions do, we maintain an allowance for loan and lease losses and other reserves to absorb the level of losses that we think is probable in our portfolios. However, our allowance for loan and lease losses may not be sufficient to cover the loan and lease losses that we actually may incur. While we maintain a reserve at a level management believes is adequate, our charge-offs could exceed these reserves. If we experience defaults by borrowers in any of our businesses to a greater extent than anticipated, our earnings could be negatively impacted.

Table of Contents

Certain of our consumer mortgage products are not sold by many financial institutions.

As a low-volume, niche-oriented originator, product design is important to differentiate us in consumer mortgage lending. We have developed our lines of business by identifying niches that we believe offer us a competitive opportunity. For this reason, the performance of our financial assets may be less predictable than those of other lenders. We may not have the same history of delinquency and loss experience to utilize in pricing and structuring some of our products as do lenders offering more seasoned asset types, and it may be more difficult to sell or securitize certain, more innovative, products.

We rely heavily on our management team and key personnel, and the unexpected loss of key managers and personnel may affect our operations adversely.

Our overall financial performance depends heavily on the performance of key managers and personnel. Our historical success was influenced strongly by our ability to attract and to retain senior management that is experienced in the niches within banking and financial services for which they are responsible. Our ability to retain executive officers and the current management teams of each of our lines of business continues to be important to implement our strategies successfully.

Ownership of our common stock is concentrated in persons affiliated with us.

Our Chairman and CEO, William I. Miller, currently has voting control, including common shares beneficially held through employee stock options that are exercisable within 60 days of January 31, 2008, of approximately 38% of our common shares. Together with Mr. Miller, directors and executive officers of Irwin beneficially own, including the right to acquire common stock through employee stock options that are exercisable within 60 days of January 31, 2008, more than 40% of our common shares. These persons likely have the ability to substantially control the outcome of all shareholder votes and to direct our affairs and business. This voting power would enable them to cause actions to be taken that may prove to be inconsistent with the interests of non-affiliated shareholders.

Our future success depends on our ability to compete effectively in a highly competitive financial services industry.

The financial services industry, including commercial banking, mortgage lending, and commercial finance, is highly competitive, and we and our operating subsidiaries encounter strong competition for deposits, loans and other financial services in all of our market areas in each of our lines of business. Our principal competitors include other commercial banks, savings banks, savings and loan associations, mutual funds, money market funds, finance companies, trust companies, insurers, leasing companies, credit unions, mortgage companies, real estate investment trusts (REITs), private issuers of debt obligations, and suppliers of other investment alternatives, such as securities firms. Many of our non-bank competitors are not subject to the same degree of regulation as we and our subsidiaries are and have advantages over us in providing certain services. Many of our competitors are significantly larger than we are and have greater access to capital and other resources, lower operating costs, and lower cost of funds. Also, our ability to compete effectively in our lines of business is dependent on our ability to adapt successfully to technological changes within the banking and financial services industry.

Our shareholder rights plan, provisions in our restated articles of incorporation, our by-laws, and Indiana law may delay or prevent an acquisition of us by a third party.

Our Board of Directors has implemented a shareholder rights plan which, combined with Indiana law, and absent the consent and approval of our Board, contain provisions which have certain anti-takeover effects. While the purpose of these plans is to strengthen the negotiating position of the Board in the event of a hostile takeover attempt, the overall

effects of the plan may be to render more difficult or to discourage a merger, tender offer or proxy contest, the assumption of control by a holder of a larger block of our shares and the removal of incumbent directors and key management. If triggered, the rights will cause substantial dilution to a person or group that attempts to acquire us without approval of our Board of Directors, and under certain circumstances, the rights beneficially owned by the person or group may become void. The plan also may have the effect of limiting the participation of certain shareholders in transactions such as mergers or tender offers whether or not such transactions are favored by incumbent directors and key management.

Table of Contents

Our restated articles of incorporation and our by-laws as well as Indiana law contain provisions that make it more difficult for a third party to acquire us without the consent of our Board of Directors. These provisions also could discourage proxy contests and may make it more difficult for you and other shareholders to elect your own representatives as directors and take other corporate actions.

Our by-laws do not permit cumulative voting of shareholders in the election of directors, allowing the holders of a majority of our outstanding shares to control the election of all our directors. We have a staggered board which means that only one-third of our board can be replaced by shareholders at any annual meeting. Directors may not be removed by shareholders. As a result of his share ownership position, our Chairman, William I. Miller, will likely be able to exercise effective control over the outcome of any shareholder vote. Our by-laws also provide that only our Board of Directors, and not our shareholders, may adopt, alter, amend and repeal our by-laws.

Indiana law provides several limitations that may discourage potential acquirers from purchasing our common shares. In particular, Indiana law prohibits business combinations with a person who acquires 10% or more of our common shares during the five-year period after the acquisition of 10% by that person or entity, unless the acquirer receives prior approval for the acquisition of the shares or business combination from our Board of Directors.

These and other provisions of Indiana law and our governing documents are intended to provide the Board of Directors with the negotiating leverage to achieve a more favorable outcome for our shareholders in the event of an offer for the Company. However, there is no assurance that these same anti-takeover provisions could have the effect of delaying, deferring or preventing a transaction or a change in control that might be in the best interest of our shareholders.

We are the defendant in class actions and other lawsuits that could subject us to material liability.

Our subsidiaries have been named as defendants in lawsuits that allege we violated state and federal laws in the course of making loans and leases. Among the allegations are that we charged impermissible and excessive rates and fees and participated in fraudulent financing. Some of these cases either seek or have attained class action status, which generally involves a large number of plaintiffs and could result in potentially increased amounts of loss. We have not established reserves for all of these lawsuits due to either lack of probability of loss or inability to accurately estimate potential loss. If decided against us, the lawsuits have the potential to affect us materially. The *Legal Proceedings* section in Part I, Item 3 of this Report describes in more detail the lawsuits in which we are named as defendants that potentially could result in material liability.

Our business may be affected adversely by Internet fraud.

We are inherently exposed to many types of operational risk, including those caused by the use of computer, internet and telecommunications systems. These may manifest themselves in the form of fraud by employees, by customers, other outside entities targeting us and/or our customers that use our internet banking, electronic banking or some other form of our telecommunications systems. Given the growing level of use of electronic, internet-based, and networked systems to conduct business directly or indirectly with our clients, certain fraud losses may not be avoidable regardless of the preventative and detection systems in place.

Our business may be affected adversely by the highly regulated environment in which we operate.

We and our subsidiaries are subject to extensive federal and state regulation and supervision. Our failure to comply with these requirements can lead to, among other remedies, administrative enforcement actions, termination or suspension of our licenses, rights of rescission for borrowers, and class action lawsuits. Legislation and regulations have had, may continue to have or may have significant impact on the financial services industry. Regulatory or

legislative changes could make regulatory compliance more difficult or expensive for us, causing us to change or limit some of our consumer loan products or the way we operate our different lines of business. Future changes could affect the profitability of some or all of our lines of business.

Our subsidiary, Irwin Union Bank and Trust, entered into a memorandum of understanding, which is considered an informal agreement, with the Federal Reserve Bank of Chicago as of March 1, 2007 to enhance the consumer compliance function and compliance oversight programs of Irwin Union Bank and Trust and its subsidiaries. Irwin Union Bank and Trust agreed to and did provide quarterly written progress reports to the Federal Reserve Bank of Chicago with respect to these matters, through the required period ending September 30, 2007. We

Table of Contents

believe we have been responsive in developing and implementing plans to address the issues raised by the Federal Reserve Bank of Chicago. We are waiting for the Federal Reserve Bank of Chicago to perform a validation of the actions we took to address their concerns. However, if the Federal Reserve Bank of Chicago concludes the actions we took are not sufficient, we could experience additional regulatory action.

The consumer lending business in which we engage is highly regulated and has been the subject of increasing legislative and regulatory initiatives. Federal, state and local government agencies and/or legislators have adopted and continue to consider legislation to restrict lenders' ability to charge rates and fees in connection with residential mortgage loans. In general, these proposals involve lowering the existing federal Homeownership and Equity Protection Act thresholds for defining a high-cost loan, and establishing enhanced protections and remedies for borrowers who receive these loans. Frequently referred to as predatory lending legislation, many of these laws and rules to which we are subject also restrict commonly accepted lending activities, such as offering balloon loan features and prepayment charges. These laws, regulations and initiatives have, and could further, limit our ability to originate consumer loans with various fees and what we believe are risk-based interest rates, and may impose additional regulatory restrictions on our business in certain states.

Because we originate home equity loans from our banking branch in Nevada, federal law permits us to charge interest rates and certain fees associated with the interest rate permitted by Nevada law regardless of where the borrowers may reside. Nonetheless, from time to time regulators and customers from other states have questioned our ability to charge certain fees, such as prepayment penalties, to residents of their states. A change in federal or state law or regulation, or an adverse interpretation or decision by a court in litigation on this issue, may affect the rates and fees we charge on home equity loans made to borrowers outside Nevada.

Our regulators have policies that can restrict the payment of cash dividends from our banking subsidiaries to us and from us to our shareholders. While we have paid dividends on our Trust Preferred, Non Cumulative Perpetual Preferred and common stock in the past, our Board has recently decided to suspend such payments. There is no certainty that we will resume such payments in the future.

Like other registrants, we are subject to the requirements of the Sarbanes-Oxley Act of 2002. Failure to have in place adequate programs and procedures could cause us to have gaps in our internal control environment, putting the Corporation and its shareholders at risk of loss.

These and other potential changes in government regulation or policies could increase our costs of doing business and could adversely affect our operations and the manner in which we conduct our business.

Item 1B. *Unresolved Staff Comments*

Not Applicable.

Item 2. *Properties*

Our main office is located at 500 Washington Street, Columbus, Indiana, in space owned by Irwin Union Bank and Trust. The location and general character of our other materially important physical properties as of January 31, 2008 are as follows:

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

simple and leases them to Irwin Union Bank and Trust. Additionally, one or the other of Irwin Union Bank and Trust or Irwin Union Realty owns the branch properties in fee at seven other locations in Bartholomew County, Indiana. These properties have no major encumbrances. Irwin Union Bank and Trust or Irwin Union Realty owns or leases nine other branch offices in Central and Southern Indiana, four offices in Michigan, two offices in Nevada, and one in Utah.

Table of Contents

Irwin Union Bank, F.S.B.

The home office is located at 500 Washington Street, Columbus Indiana. Irwin Union Bank, F.S.B. has eleven branch offices located in Arizona(2), California (2), Florida, Kentucky, Missouri, Nevada, Ohio, New Mexico and Wisconsin. All 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 Commercial Finance Corporation, Equipment Finance, formerly Irwin Business Finance Corporation is in Bellevue, Washington and is leased. Our Canadian commercial finance subsidiary, Irwin Commercial Finance Canada Corporation (formerly Onset Capital Corporation), leases its main office in 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 in Montvale, New Jersey and Purchase, New York and are both leased. The franchise subsidiary also leases office space in Columbus, Ohio. In addition, Irwin Franchise Capital owns the building that houses its telesales center in Columbus, Nebraska.

Irwin Home Equity

The main office is located at 12677 Alcosta Boulevard, Suite 500, San Ramon, California. Irwin Home Equity occupies one other office at this location and an office in Charlotte, North Carolina. All three offices are leased.

Irwin Mortgage

The bulk of the remaining activities of this discontinued operation are conducted from an office located at 10500 Kincaid Drive, Fishers, Indiana, which is leased.

Item 3. *Legal Proceedings*

Culpepper v. Inland Mortgage Corporation

On February 29, 2008, the United States Court of Appeals for the 11th Circuit denied the plaintiffs' petition for rehearing and petition for rehearing en banc. The denial let stand the 11th Circuit's July 2, 2007 affirmation of the district court's decision in favor of our indirect subsidiary Irwin Mortgage Corporation (formerly Inland Mortgage Corporation). This lawsuit was filed in April 1996 in the United States District Court for the Northern District of Alabama, seeking class action status and alleging Irwin Mortgage's payment of broker fees to mortgage brokers violated the federal Real Estate Settlement Procedures Act. In its July 2, 2007 decision affirming summary judgment in favor of Irwin Mortgage, the court of appeals held that plaintiffs had failed to show that the total compensation Irwin Mortgage paid to the mortgage brokers was unreasonable in light of the services provided. The court of appeals also held that the district court had not abused its discretion in decertifying the plaintiffs' class because individual issues predominated, making class certification inappropriate. The plaintiffs have until May 29, 2008 to file a petition for a writ of certiorari seeking discretionary review by the United States Supreme Court. This action will conclude if a petition for certiorari is not filed, or is denied. We have not established any reserves for this case.

Cohens v. Inland Mortgage Corporation

In October 2003, our indirect subsidiary, Irwin 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,

alleged they were injured from lead contamination while living in premises allegedly owned by the defendants. The suit sought approximately \$41 million in damages and alleged negligence, breach of implied warranty of habitability and fitness for intended use, loss of services and the cost of medical treatment. On February 1, 2008, the parties agreed in principle to settle this case for a nonmaterial amount, subject to approval by the court.

Table of Contents

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 class 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. On September 9, 2005, the *Kossler* plaintiffs filed a Third Amended Class Action Complaint. On October 21, 2005, Irwin filed a renewed motion seeking to dismiss the *Kossler* action.

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 September 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 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. On September 17, 2004, Irwin made a demand for indemnification and a defense to *Hobson, Chatfield* and *Ransom*. Community denied this request as premature.

In response to a motion by Irwin, the Judicial Panel On Multidistrict Litigation consolidated *Hobson, Chatfield* and *Ransom* with *Kessler* in the Western District of Pennsylvania for all pretrial proceedings. The Pennsylvania District Court had been handling another case seeking class action status, *Kessler v. RFC, et al.*, also involving

Table of Contents

Community and with facts similar to those alleged in the Irwin consolidated cases. The *Kessler* case had been settled, but the settlement was appealed and set aside on procedural grounds. Subsequently, the parties in *Kessler* filed a motion for approval of a modified settlement, which would provide additional relief to the settlement class. Irwin is not a party to the *Kessler* action, but the resolution of issues in *Kessler* may have an impact on the Irwin cases. The Pennsylvania District Court has effectively stayed action on the Irwin cases until issues in the *Kessler* case are resolved. On January 25, 2008, the Pennsylvania District Court approved and certified for settlement purposes the modified *Kessler* settlement, finding the proposed modified *Kessler* settlement to be fair and reasonable, and directed the parties to supply a proposed notice plan. We have established an immaterial reserve for the Community litigation based upon SFAS 5 guidance and the advice of legal counsel.

Putkowski v. Irwin Home Equity Corporation and Irwin Union Bank and Trust Company

On August 12, 2005, our indirect subsidiary, Irwin Home Equity Corporation, and our direct subsidiary, Irwin Union Bank and Trust Company (collectively, Irwin), were named as defendants in litigation seeking class action status in the United States District Court for the Northern District of California for alleged violations of the Fair Credit Reporting Act. In response to Irwin's motion to dismiss filed on October 18, 2005, the court dismissed the plaintiffs complaint with prejudice on March 23, 2006. Plaintiffs filed an appeal in the U.S. Court of Appeals for the 9th Circuit on April 13, 2006. On January 25, 2008, the parties agreed in principle to settle this litigation for a nonmaterial amount.

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.

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

During the fourth quarter of 2007, no matters were submitted to a vote of our security holders, through the solicitation of proxies or otherwise.

Table of Contents**PART II****Item 5. *Market for Registrant's Common Equity, Related Stockholder Matters, and Issuer Purchases of Equity Securities.***

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 March 7, 2008, was 1,831.

Stock Prices and Dividends:

	Price Range		Quarter	Cash	Total
	High	Low	End	Dividends	Dividends
					For Year
2006					
First quarter	\$ 21.96	\$ 19.10	\$ 19.33	\$ 0.11	
Second quarter	21.20	17.92	19.39	0.11	
Third Quarter	20.25	18.08	19.56	0.11	
Fourth Quarter	23.00	19.34	22.63	0.11	\$ 0.44
2007					
First quarter	\$ 22.95	\$ 18.21	\$ 18.64	\$ 0.12	
Second quarter	18.74	14.63	14.97	0.12	
Third Quarter	15.75	9.32	11.02	0.12	
Fourth Quarter	12.21	7.21	7.35	0.12	\$ 0.48

On February 28, 2008, the Board of Directors elected to defer dividend payments on the Corporation's trust preferred securities and elected to discontinue payment of dividends on its non-cumulative perpetual preferred and common stock. These steps are being undertaken to maintain the capital strength of the Corporation at a time of elevated uncertainty in the economy.

Interest on the subordinated debt underlying the trust preferred securities will continue to accrue at its scheduled rate and cash dividends will be paid to holders prior to the resumption of dividends on the non-cumulative perpetual preferred and common stock.

The Board took action on the perpetual preferred and common stock as it believes, in a total stakeholder balance, that the elevated uncertainty in the current environment demands a greater bias to capital retention on a precautionary basis than distribution of cash from retained earnings for maintenance of historic dividends.

The Board will reassess its dividend policy regularly, with an eye towards resuming the cash payment of the deferred dividends on trust preferred securities and recommencing dividends on the non-cumulative perpetual preferred and common stock once the level of uncertainty in the current market declines and the profitability of the Corporation supports such dividends. The ability to pay future dividends will be subject to the regulatory restrictions discussed above.

Sales of Unregistered Securities:

There were no sales of unregistered securities.

Issuer Purchases of Equity Securities:

In 2006, the Board of Directors of the Corporation approved the repurchase of up to two million shares or up to \$50 million of common stock of the Corporation. In 2006 and in early 2007, we repurchased \$15 million through this plan. Due to our operating losses and deteriorating conditions in the capital markets, we discontinued our

Table of Contents

common stock repurchases. We do not plan on repurchasing common stock in the foreseeable future. The following table shows our repurchase activity for the past three months:

Calendar Month	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plan or Program	Approximate Dollar Value of Shares that May Yet Be Purchased under the Plan or Program
October		\$		\$ 34,977,252
November				\$ 34,977,252
December		\$		\$ 34,977,252
Total		\$		\$ 34,977,252

Item 6. Selected Financial Data**Five-Year Selected Financial Data**

The figures in the table below are for Continuing Operations and, unless otherwise indicated, specifically exclude results for those operations now designated Discontinued Operations (see Footnote 2 in the Notes to the Consolidated Financial Statements).

	2007	At or For Year Ended December 31,			2003
		2006	2005	2004	
		(Dollars in thousands except per share data)			
For the year:					
Net revenues	\$ 154,789	\$ 266,959	\$ 260,881	\$ 283,994	\$ 135,175
Noninterest expense	199,767	210,688	204,039	203,778	144,637
Income (loss) before income taxes	(44,978)	56,271	56,842	80,216	(9,462)
Provision for income taxes	(20,848)	18,870	20,595	31,492	(5,321)
Net (loss) income from continuing operations	(24,130)	37,401	36,247	48,724	(4,141)
(Loss) income from discontinued operations	(30,543)	(35,674)	(17,260)	19,721	76,958
Net (loss) income	\$ (54,673)	\$ 1,727	\$ 18,987	\$ 68,445	\$ 72,817

Common Share Data:Earnings per share from
continuing operations:

Basic	\$ (0.87)	\$ 1.27	\$ 1.27	\$ 1.72	\$ (0.15)
Diluted	(0.90)	1.25	1.26	1.64	(0.15)
Cash dividends per share	0.48	0.44	0.40	0.32	0.28
Book value per common share	15.22	17.30	17.90	17.61	15.36
Dividend payout ratio ⁽¹⁾	(25.69)%	759.12%	60.18%	13.24%	10.76%
Weighted average shares basic	29,337	29,501	28,518	28,274	27,915
Weighted average shares diluted	29,344	29,690	28,841	31,278	28,240
Shares outstanding end of period	29,226	29,736	28,618	28,452	28,134

At year end:

Assets	\$ 6,166,105	\$ 6,237,958	\$ 6,646,524	\$ 5,235,820	\$ 4,988,359
Residual interests	12,047	10,320	22,116	56,101	71,491
Loans held for sale	6,134	237,510	513,554	227,880	204,535
Loans and leases	5,696,230	5,238,193	4,477,943	3,440,689	3,147,094
Allowance for loan and lease losses	144,855	74,468	59,223	43,441	63,005
Servicing assets	23,234	31,949	34,445	47,807	31,949
Deposits	3,325,488	3,551,516	3,898,993	3,395,263	2,899,662
Other borrowings	802,424	602,443	997,444	237,277	429,758
Collateralized debt	1,213,139	1,173,012	668,984	547,477	590,131
Other long-term debt	233,873	233,889	270,160	270,172	270,184
Shareholders equity	459,300	530,502	512,334	501,185	432,260

Table of Contents

At or For Year Ended December 31,
2007 2006 2005 2004 2003
(Dollars in thousands except per share data)

Selected Financial Ratios:*Performance Ratios on continuing operations:*

Return on average assets	(0.4)%	0.6%	0.6%	0.9%	(0.1)%
Return on average equity	(4.8)	7.1	7.5	10.3	(1.1)
Net interest margin ⁽²⁾	4.50	4.71	4.97	5.46	5.82
Noninterest income to revenues ⁽³⁾	9.5	14.8	19.7	28.6	(10.7)
Efficiency ratio ⁽⁴⁾	68.9	69.8	70.8	68.3	79.4
Loans and leases and loans held for sale to deposits ⁽⁵⁾	126.4	117.3	108.0	80.7	87.1
Average interest-earning assets to average interest-bearing liabilities	112	119	126	132	132

Asset Quality Ratios:

Allowance for loan and lease losses to:

Total loans and leases	2.5%	1.4%	1.3%	1.3%	2.0%
Non-performing loans and leases	190	199	158	129	142
Net charge-offs to average loans and leases	1.2	0.5	0.3	0.7	1.1
Non-performing assets to total assets	1.5	0.9	0.8	0.9	1.1
Non-performing assets to total loans and leases and other real estate owned	1.6	1.0	1.2	1.3	1.7

Ratio of Earnings to Fixed Charges:

Including deposit interest	0.8x	1.2x	1.4x	2.0x	0.9x
Excluding deposit interest	0.6	1.5	2.1	3.3	0.8

Capital Ratios:

Average shareholders' equity to average assets	8.3%	8.1%	8.0%	9.0%	7.6%
Tier 1 capital ratio	10.2	11.4	10.7	13.0	11.4
Tier 1 leverage ratio	10.2	11.5	10.3	11.6	11.2
Total risk-based capital ratio	12.6	13.4	13.1	15.9	15.1

- (1) Dividends paid as a percentage of earnings from total operations.
- (2) Net interest income divided by average interest-earning assets.
- (3) Revenues consist of net interest income plus noninterest income.
- (4) Noninterest expense divided by net interest income plus noninterest income.
- (5) Excludes first (but not second) mortgage loans held for sale and loans collateralizing secured financings.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Strategy

Our strategy is to position the Corporation as an interrelated group of specialized financial services companies serving niche markets of small businesses and consumers while optimizing the productivity of our capital. We seek to create competitive advantage within the banking industry by serving small businesses and consumers with lending, leasing, deposit, advisory services and specialized mortgage products. Our strategic objective is to create value through well-controlled, profitable growth by attracting, retaining and developing exceptional management teams at our lines of business and parent company who focus on (i) meeting customer needs rather than simply offering banking products or services, (ii) being cost-efficient in our delivery, and (iii) having strong risk

Table of Contents

management systems. We believe we must continually balance these three factors in order to deliver long-term value to all of our stakeholders.

We have developed several tactics to meet these goals:

1. *Identify market niches.* Based on our assessment of long-term market, customer and competitive trends and opportunities, we focus on product or market niches in banking for small businesses and consumers where our understanding of customer needs and ability to meet them creates added value that permits us not to have to compete primarily on price. We do not believe it is necessary to be the largest or leading market share company in any of our product lines to earn an adequate risk-adjusted return, but we do believe it is important that we are viewed as a preferred provider of those product offerings in our niche segments. At present we provide small businesses and consumers with lending, leasing, deposit, advisory services and specialized mortgage products.

2. *Attract, develop and retain exceptional management with niche expertise.* We participate in lines of business only when we have attracted senior managers who have proven track records in the niche for which they are responsible. Our structure allows managers to focus their efforts on understanding their customers, meeting the needs of the markets they serve cost effectively, and identifying and controlling the risks inherent in their activities. This structure also promotes accountability among managers of each segment. We attempt to create a mix of short-term and long-term rewards that provide these managers with the incentive to achieve well-controlled, profitable growth over the long term.

3. *Diversify capital and earnings risk.* We diversify our revenues, credit risk, and application of capital across complementary lines of business and across different regions as a key part of our risk management. For example, the customers of our commercial bank have different growth and risk profiles in the Midwest and West. These markets perform differently due to differences in local economies, affecting both demand and credit quality of our products. Our home equity segment lends to consumers on a national basis, building a diversified portfolio where demand and credit quality fluctuate depending, in part, on local market conditions. Our customers' credit needs 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.

4. *Focus on organic growth.* We primarily focus on growth through organic expansion of existing lines of business as we believe this approach often provides a better risk/return profile. Over the past ten years, we have made only a few acquisitions. Those have typically not been in competitive bidding situations.

5. *Identify opportunities for coordination and efficiencies across the Bank.* We have recently increased our attention to the identification of areas in which we can better coordinate and consolidate non-customer facing operations within our segments. Our objective is to improve risk management and operating efficiency without diminishing our ability to provide a high level of service to our customers. Our efforts to date have focused on the centralization of certain risk management functions, as well as improvements in information technologies, procurement, and transactional accounting through shared services.

6. *Create and maintain risk management systems appropriate to our size, scale and scope.* These systems are an integral part of a well-managed banking organization and are as important to our future success as hiring good people and offering products and services in attractive niches. We are engaged in a multiyear process of enhancing our management depth and systems for assuring that we operate our businesses within the risk appetite established by our board of directors. The system we are creating provides centralized guidance and support from staff with demonstrated risk management expertise, who provide an independent perspective assessing and assisting the risk management processes and systems that are an integral part of each of our managers' responsibilities.

We believe long-term growth and profitability will result from our endeavors to serve attractive niches within commercial and consumer banking, our experienced management, our diverse products and geographic markets, and our focus on risk management systems.

Table of Contents

Outlook

We expect to return to profitability by the second half of the year and possibly sooner. Depending primarily on the delinquency and charge-off levels in our home equity and commercial banking portfolios (and the additions to the allowance for loans and lease losses driven by those statistics), we believe profitability in the second half of the year should be enough to make us profitable for the full year in 2008.

The substantial loss we sustained in 2007 can be directly traced to the unprecedented dislocation in the housing markets (and a spike in mortgage repurchase demands at our Discontinued Operations in the third quarter), rising unemployment, and less liquidity in certain portions of the credit markets. While only the rise in repurchase demands has abated so far, the steps taken during 2007 to increase our reserves and decrease our operating expenses should enable us to return to profitability.

We have three principal financial goals this year:

1. As noted above, the first is to return to profitability. Given current and predicted conditions in the economy, we believe this is achievable, although our plans indicate a level of profitability well below our long-term targets.
2. Manage our balance sheet to maintain strong capital and good liquidity through this period of economic stress.
3. Manage our credit relationships and servicing and collections platforms to minimize our credit loss exposures.

In 2006, we reached a conclusion about the commoditization and irrational pricing of the first mortgage business. Accordingly, we sold our interests in that segment. We were not, however, able to predict the severity or widespread nature of the losses sustained over the past two years, driven by the unexpectedly rapid and dramatic changes in the residential housing markets, borrower attitudes about defaulting on their mortgages, and borrower fraud. In times of elevated uncertainty, few can make accurate predictions. We believe the most appropriate response to the current economic environment is to plan conservatively and carefully in case conditions do not improve soon.

As such, over the past several quarters we have focused on constraining balance sheet growth and reducing overall operating expenses, while strengthening our credit underwriting, servicing, collections, and risk management areas. This has had a drag on recent results, but we think our actions position us for improved results in 2008. In addition, we have added substantially to loss reserves. In 2007 we added \$135 million to reserves, more than double our actual losses of \$64 million. This addition to reserves has increased the ratio of reserves to loans and leases from 1.4 percent to 2.5 percent. If our assumptions about the degree to which actual (i.e., realized) losses will increase in 2008 due to economic conditions prove true, these reserves — the expense for which we have already recognized — will help in managing our way to profitability in spite of a difficult economic environment.

Our consumer segments — home equity and discontinued operations — had substantial losses in 2007. We believe 2008 will be better in both.

In our home equity segment, we had several set-backs in 2007.

1. Secondary market liquidity for non-conforming mortgage products shut-down in 2007. As a risk-mitigation step, we accelerated the securitization of loans in the second quarter and were able to match-fund \$300 million of loans prior to that market collapsing in the summer.

This securitization, like most we have done in this segment, has served to limit our risk of catastrophic loss. This is a very important risk mitigating factor in sizing our ultimate risk to defaults in this segment. Please refer to the section

on Home Equity Servicing and Credit Quality in the discussion of the home equity segment for additional information. In short, while we bear some risk of loss on these securitized loans, our loss is limited to the degree of overcollateralization we accepted in selling the loans to the securitization trusts. We are not obligated to, nor do we expect that we would, support the bonds issued by these trusts by providing cash or other security interest to the trusts in the future should the underlying home equity loan performance be insufficient to support debt service to bondholders. In addition, it should be noted that such a potential debt service short-fall to the

Table of Contents

bondholders would not be considered an event of default by Irwin as we are not the obligors on these securitization bonds. As of December 31, 2007, the overcollateralization embedded in the home equity securitization trusts, or the amount we have risk to future losses, totaled approximately \$150 million.

2. The lack of secondary market liquidity in the second half of the year (and continuing into 2008) meant, however, that we needed to modify our product offerings significantly and limit our production to the amount we wished to hold on balance sheet. This significantly reduced our production and led us to meaningfully reduce staff. In total, we reduced staff (FTE s) by 152 or 31 percent, incurring severance-related charges of \$4 million. In this segment, we have reduced our annualized non-interest expense by about \$12 million.
3. A disproportionate share of our realized and expected losses have arisen from a portfolio we originated prior to 2007 and held in for sale classification in early 2007. These loans were underwritten to third-party credit guidelines and as mortgage market conditions deteriorated in 2007, these third-party buyers left the market. We ceased origination of these types of loans as soon as secondary market outlets for them were withdrawn. Rather than selling into a depressed market, we reclassified these loans, approximately \$167 million, into held-for-investment status, having marked them to then current market. Throughout 2007, the credit quality of these loans continued to deteriorate, leading to heightened charge-offs and higher provisions.

These issues notwithstanding, we now have a smaller, but very motivated team in this segment, a highly-rated servicing platform, and we believe, a good opportunity, with some stabilization in the housing markets, to lower our losses in 2008 particularly in the second half of the year and possibly sooner. This segment is unlikely to return to profitability until delinquencies in its portfolio not only cease to rise, but start to fall meaningfully. At the present time, we cannot predict when that will be. However, even reducing our loss in the home equity segment should allow consolidated results to return solidly to profitability. Until the residential real estate markets in the US normalize and we can assess the long-term attractiveness of the mortgage markets, we will continue to limit production in this segment and seek to reduce the size of our home equity portfolio over time.

In our Discontinued Operations, we have largely wound-up operational issues, but took significant charges in 2007 to reserve for loan repurchase risks, reflecting a spike in repurchase demands in the third quarter. Our reserve held-up well with no additional repurchase reserves needed in the fourth quarter. The risk of needing additional reserves is declining as time passes; it has been nearly a year and a half since we originated our last loan in this segment. We are maintaining a limited number of qualified staff who continue to manage our residual liabilities and responsibilities from prior activities.

We expect our commercial banking segment to have improved results in 2008, but the degree of improvement will depend on economic conditions in their principal markets in the Midwest and West. In 2007, slow deposit and loan growth, excess staffing, narrowing net interest margins, and increases in our loan loss provision including covering the costs of a loan fraud which accounted for nearly 40 percent of the 2007 losses in this segment all contributed to a disappointing year. Through selective staff reductions and strengthening of our capabilities in areas such as deposit sales, we believe net income can increase, notwithstanding what we believe will be difficult economic headwinds and higher credit costs.

Finally, we also anticipate income growth in our commercial finance segment. This portion of the Corporation has performed well by managing the environment with good product positioning, credit quality, and healthy net interest margins.

The past two years have been very challenging for our organization. We have taken a number of steps to maintain our financial strength throughout the period. As a result, we are in a good capital and liquidity position to weather the current difficult environment for banks. For example:

Our lead bank, Irwin Union Bank and Trust, began the year 2007 with a risk-weighted capital ratio of 12.8 percent. In spite of losing \$45 million in 2007, the Bank ended the year with a risk-weighted capital ratio of 12.5 percent. This compares to our Capital Policy Limit of 12.0 percent. We maintained this strong

Table of Contents

capital by proactively reducing our balance sheet to maintain capital ratios above our internal limits through asset sales, participations, credit tightening, production limitations and run off.

We have a Liquidity Policy and liquidity contingency plans which have been in place for several years. These have been functioning well in this time of stress. The primary metric used in liquidity planning is Available-But-Unused Funds or ABU. While ABU has declined in the past year, principally reflecting the loss of escrow deposits as the Corporation reduced its risk profile by selling substantially all its Mortgage Servicing Rights (MSRs), liquidity remained good. The current level of ABU is in excess of \$500 million, comfortably above the Board's policy limit for ABU of \$375 million.

Our Board of Directors has taken added steps to help ensure we have a strong capital base with which to weather the uncertainties in the current market and outlook. The Board has elected to defer dividend payments on the Corporation's trust preferred securities and elected to discontinue payment of dividends on its non-cumulative perpetual preferred and common stock to further bolster capital. The Board took these actions as it believes, in a total stakeholder balance, that the elevated uncertainty in the current environment demands a greater bias to capital retention on a precautionary basis than to distribution of cash from retained earnings for maintenance of historic dividends.

Our current outlook for 2008 is that we will return to profitability. The Board will reassess its dividend policy regularly with an eye towards resuming the cash revenue of the deferred dividends on trust preferred securities and recommencing dividends on the non-cumulative perpetual preferred and common stock once the level of uncertainty in the current market declines and the profitability of the Corporation supports such dividends. The ability to pay future dividends will be subject to the regulatory restrictions discussed above.

Critical Accounting Policies/Management Judgments and Accounting Estimates

Accounting estimates are an integral part of our financial statements and are based upon data analysis and 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

When we securitize or sell loans, we may retain the right to service the underlying loans sold. For cases in which we retain servicing rights, a portion of the cost basis of loans sold is allocated to a servicing asset based on its fair value relative to the loans sold and the servicing asset combined. Servicing rights associated with first mortgages are carried at lower of cost or fair market value. We use a combination of observed pricing on similar, market-traded servicing rights and internal valuation models that calculate the present value of future cash flows to determine the fair value of the servicing assets. These models are supplemented and calibrated to market prices using inputs from independent servicing brokers, industry surveys and valuation experts. In using this valuation method, we incorporate assumptions that we believe market participants would use in estimating future net servicing income, which include, among other items, estimates of the cost of servicing per loan, the discount rate, float value, an inflation rate, ancillary income per loan, prepayment speeds, and default rates.

For servicing assets associated with second mortgages and high loan-to-value first mortgages, the fair value measurement method of reporting these servicing rights was elected beginning January 1, 2007, in accordance with SFAS 156, Accounting for Servicing of Financial Assets. Under the fair value method, we measure servicing assets at fair value at each reporting date and report changes in fair value in earnings in the period in which the changes occur.

All remaining servicing rights follow the amortization method for subsequent measurement whereby these servicing rights are amortized in proportion to and over the period of estimated net servicing income.

Table of Contents

Allowance for Loan and Lease Losses and Repurchase Reserves

The allowance for loan and lease losses (ALLL) is an estimate based on management's 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. The allowance is maintained at a level we believe is adequate to absorb probable losses inherent in the loan and lease portfolio. We perform an assessment of the adequacy of the allowance on a quarterly basis.

Within the allowance, there are specific and expected loss components. The specific loss component is assessed for loans we believe to be impaired in accordance with 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 of that loan. 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 indicates that certain losses exist. 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.

It is our policy to promptly charge off any loan, or portion thereof, which is deemed to be uncollectible. This includes, but is not limited to, any loan rated Loss by the regulatory authorities. Impaired commercial credits are considered on a case-by-case basis. The amount charged off includes any accrued interest. Unless there is a significant reason to the contrary, consumer loans are charged off when deemed uncollectible, but generally no later than when a loan is past due 180 days.

See the Credit Risk section of Management's Discussion and Analysis and Footnote 6 to the consolidated financial statements for further discussion.

In addition to the ALLL, at our discontinued mortgage banking segment we have recorded a reserve for potential losses resulting from repurchases in instances where there were origination errors. Such errors include inaccurate appraisals, errors in underwriting, and ineligibility for inclusion in loan programs of government-sponsored entities which programs relieve us of future credit losses. In determining reserve levels for repurchases, we estimate the number of loans with origination 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.

Accounting for Deferred Taxes

Deferred tax assets and liabilities are the expected future tax amounts for the temporary differences between carrying amounts and tax basis of assets and liabilities, computed using enacted tax rates. 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, in part, based on estimates of future taxable income. Events may occur in the future that could cause the ability to realize these deferred tax assets to be in doubt, requiring the need for a valuation allowance.

Incentive Servicing Fees

For whole loan sales of certain home equity loans, in addition to our normal servicing fee, we have the right to an incentive servicing fee (ISF) that will provide cash payments to us if a pre-established return for the certificate holders

and certain structure-specific loan credit and servicing performance metrics are met. Generally the structure-specific metrics involve both a delinquency and a loss test. The delinquency test is satisfied if, as of the last business day of the preceding month, delinquencies on the current pool of mortgage loans are less than or equal to a given percentage. The loss test is satisfied if, on the last business day of the preceding month, the percentage of cumulative losses on the original pool of mortgage loans is less than or equal to the applicable percentage as outlined in the specific deal documents. We receive ISF payments monthly once the pre-established

Table of Contents

return has been paid to the certificate holder, if the delinquency and loss percentages are within guidelines. If we are terminated or replaced for cause as servicer under the securitization, the cash flow stream under the ISF contract terminates.

We account for ISFs similar to management contracts under Emerging Issues Task Force Topic No. D-96, Accounting for Management Fees Based on a Formula. Accordingly, we recognize revenue on a cash basis as the pre-established performance metrics are met and cash is due.

Consolidated Overview

	2007	% Change	2006	% Change	2005
Net (loss) income from continuing operations (millions)	\$ (24.1)	(165)%	\$ 37.4	3%	\$ 36.2
Net (loss) income (millions)	(54.7)	(3,266)%	1.7	(91)%	19.0
Basic earnings per share from continuing operations	(0.87)	(169)%	1.27	0%	1.27
Basic earnings per share	(1.91)	(3,283)%	0.06	(91)%	0.67
Diluted earnings per share from continuing operations	(0.90)	(172)%	1.25	(1)%	1.26
Diluted earnings per share	(1.94)	(3,980)%	0.05	(92)%	0.66
Return on average equity from continuing operations	(4.8)%		7.1%		7.5%
Return on average assets from continuing operations	(0.4)%		0.6%		0.6%

As discussed below, the financial statements, footnotes, schedules and discussion within this report conform to the presentation required for discontinued operations pursuant to the sale of our mortgage banking line of business and specifically exclude results for those operations now designated Discontinued Operations (see Footnote 2 of the Notes to the Consolidated Financial Statements).

Consolidated Income Statement Analysis*Net Income from Continuing Operations*

We recorded a net loss from continuing operations of \$24 million for the year ended December 31, 2007, down from net income from continuing operations of \$37 million for the year ended December 31, 2006, and \$36 million in 2005. Net loss per share (diluted) from continuing operations was \$0.90 for the year ended December 31, 2007, down from income of \$1.25 per share in 2006 and \$1.26 per share in 2005. Return on equity from continuing operations was (4.8)% for the year ended December 31, 2007, 7.1% in 2006 and 7.5% in 2005. The decrease in 2007 earnings from continuing operations relates to the significant deterioration of the mortgage markets. This disruption led to large losses in the home equity segment as a result of increasing provision for loans losses. During 2007, we provided \$135 million in loan loss provision compared to \$35 million in 2006 and \$27 million in 2005. This provision is based on significant revisions in our expectations of future losses that have not yet been incurred. We believe these reserves adequately reflect our risk of loss in the current and expected environment. Our need for higher or lower reserves will change as likelihood of customer defaults changes.

Net Interest Income from Continuing Operations

Net interest income from continuing operations for the year ended December 31, 2007 totaled \$262 million, up 2% from 2006 net interest income from continuing operations of \$257 million and up 13% from 2005.

Table of Contents

The following table shows our daily average consolidated balance sheet and interest rates at the dates indicated. We do not show interest income on a tax equivalent basis because it is not materially different from the results in the table.

	2007		December 31, 2006				2005	
	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate	Average Balance	Interest
	(Dollars in thousands)							
Assets								
Operating assets:								
Operating deposits with								
Substitutions	\$ 49,587	\$ 2,668	5.38%	\$ 72,110	\$ 2,925	4.06%	\$ 80,508	\$ 1,816
Bills sold	13,765	619	4.50	30,419	1,527	5.02	15,064	387
Interests	10,458	1,100	10.52	13,512	1,536	11.37	39,942	6,948
Securities	138,866	7,647	5.51	117,164	5,816	4.96	107,220	5,813
For sale	95,815	6,843	7.14	865,061	73,708	8.52	1,217,367	94,324
Leases, net of income ⁽¹⁾	5,486,727	496,101	9.04	4,872,487	437,900	8.99	3,890,077	312,970
Non-earning assets:								
Cash and cash equivalents	5,795,218	\$ 514,978	8.89%	5,970,753	\$ 523,412	8.77%	5,350,178	\$ 422,258
Loans from banks	74,438			111,382			109,837	
Land and equipment, net	38,926			34,349			30,543	
Goodwill	286,597			470,845			572,028	
Allowance for loan and losses	(92,889)			(67,383)			(50,322)	
	\$ 6,102,290			\$ 6,519,946			\$ 6,012,264	
Liabilities and Shareholders' Equity								
Operating liabilities:								
Demand checking	\$ 285,618	\$ 6,320	2.21%	\$ 355,378	\$ 8,490	2.39%	\$ 479,621	\$ 9,789
Demand savings	1,159,705	50,409	4.35	1,169,465	48,673	4.16	1,118,655	29,631
Time deposits	122,666	2,675	2.18	131,182	2,481	1.89	119,349	1,547
Borrowings	1,531,307	77,956	5.09	1,558,128	72,576	4.66	1,204,421	42,894
Long-term debt	598,888	31,117	5.20	543,719	33,663	6.19	421,085	21,244
Short-term debt	1,233,604	68,601	5.56	1,005,959	53,720	5.34	629,503	25,587
Other term debt	233,916	17,335	7.41	246,948	22,486	9.11	290,188	25,676
Non-earning liabilities:								
Demand deposits	\$ 5,165,704	\$ 254,413	4.93%	\$ 5,010,779	\$ 242,089	4.83%	\$ 4,262,822	\$ 156,368
Time deposits	329,925			756,624			989,234	
Other liabilities	101,067			226,379			279,784	
Shareholders' equity	505,594			526,164			480,424	
	\$ 6,102,290			\$ 6,519,946			\$ 6,012,264	

ities and s equity			
income	\$ 260,565	\$ 281,323	\$ 265,890
income to average ing assets	4.50%	4.71%	
income from d operations	(1,828)	23,884	34,423
income from operations	\$ 262,393	\$ 257,439	\$ 231,467

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

Table of Contents

Net interest margin for the year ended December 31, 2007 was 4.50% compared to 4.71% in 2006 and 4.97% in 2005. The decline in margin in 2007 relates to our increasing cost of funds which have risen at a faster pace than our yields on loans. This reflects competitive conditions for both assets and liabilities, liability rate stickiness in a declining rate environment in the second half of 2007, and the loss of low-cost escrow deposits that were associated with mortgage servicing rights in our Discontinued Operations. 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,					
	2007 Over 2006			2006 Over 2005		
	Volume	Rate	Total	Volume	Rate	Total
	(Dollars in thousands)					
Interest Income						
Loans and leases	\$ 55,203	\$ 2,998	\$ 58,201	\$ 79,038	\$ 45,892	\$ 124,930
Mortgage loans held for sale	(65,543)	(1,321)	(66,864)	(27,297)	6,681	(20,616)
Investment securities	1,077	752	1,829	539	(536)	3
Residual interests	(347)	(90)	(437)	(4,598)	(814)	(5,412)
Interest bearing deposits with financial institutions	(914)	657	(257)	(189)	1,298	1,109
Federal funds sold	(835)	(71)	(906)	396	744	1,140
Total	(11,359)	2,925	(8,434)	47,889	53,265	101,154
Interest Expense						
Money market checking	(1,666)	(504)	(2,170)	(2,536)	1,237	(1,299)
Money market savings	(406)	2,142	1,736	1,346	17,696	19,042
Regular savings	(161)	354	193	153	781	934
Time deposits	(1,249)	6,630	5,381	12,596	17,086	29,682
Other borrowings	3,415	(5,960)	(2,545)	6,187	6,232	12,419
Collateralized debt	12,157	2,724	14,881	15,302	12,831	28,133
Other long-term debt	(1,187)	(3,965)	(5,152)	(3,826)	636	(3,190)
Total	10,903	1,421	12,324	29,222	56,499	85,721
Net Interest Income	\$ (22,262)	\$ 1,504	\$ (20,758)	\$ 18,667	\$ (3,234)	\$ 15,433

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 from Continuing Operations

The consolidated provision for loan and lease losses for the year 2007 was \$135 million, compared to \$35 million and \$27 million in 2006 and 2005, respectively. More information on this subject is contained in the section on Credit Risk.

Noninterest Income from Continuing Operations

Noninterest income during the year 2007 totaled \$27 million, compared to \$45 million for 2006 and \$57 million in 2005. The decrease in 2007 versus 2006 related primarily to lower servicing revenues, net of amortization and impairment, and to derivative losses on foreign currency contracts associated with our small-ticket leasing business in Canada. We recorded offsetting foreign currency transaction gains in the noninterest expense section of the income statement.

Table of Contents*Noninterest Expense from Continuing Operations*

Noninterest expenses for the year ended December 31, 2007 totaled \$200 million, compared to \$211 million in 2006 and \$204 million in 2005. The decrease in consolidated noninterest expense in 2007 is primarily related to foreign currency transaction gains related to our small-ticket leasing business in Canada as well as decreases at our home equity lending business related to variable compensation costs, all of which offset severance and restructuring costs in our home equity, commercial banking, and parent segments.

Consolidated Balance Sheet Analysis

Total assets at December 31, 2007 were \$6.2 billion, down 1% from December 2006. Average assets for 2007 were \$6.1 billion down 6% from 2006, and down 1% from 2005. The decline in the average consolidated balance sheet reflects the sale of our mortgage banking line of business assets, offset only in part by growth in our commercial portfolios as we sought to manage the size of our balance sheet in the wake of poor financial results.

Investment Securities

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

	2007	2006	2005
	(Dollars in thousands)		
U.S. Treasury and government obligations	\$ 13,970	\$ 13,730	\$ 12,571
Obligations of states and political subdivisions	3,436	3,545	3,544
Mortgage-backed securities	46,216	45,187	28,331
Other	14,185	3,380	3,199
Total	77,807	65,842	47,645
Federal Home Loan Bank and Federal Reserve Bank stock	62,588	62,588	69,697
Total	\$ 140,395	\$ 128,430	\$ 117,342

The following table shows maturity distribution of our investment securities at December 31, 2007:

	Within One Year	After One But Within Five Years	After Five But Within Ten Years	After Ten Years	Other	Total
	(Dollars in thousands)					
U.S. Treasury and government obligations	\$ 4,229	\$ 9,741	\$ 620	\$ 2,816	\$ 3,436	\$ 13,970

Obligations of states and political subdivisions						
Other				14,185		14,185
Total	4,229	9,741	620	17,001		31,591
Mortgage-backed securities					46,216	46,216
Federal Home Loan Bank and Federal Reserve Bank stock					62,588	62,588
	\$ 4,229	\$ 9,741	\$ 620	\$ 17,001	\$ 108,804	\$ 140,395
Weighted Average Yield						
Held-to-maturity	3.30%	3.65%	5.20%	5.35%	5.72%	
Available-for-sale	4.14%				5.00%	

Average yield represents the weighted average yield to maturity computed based on amortized cost balances. The yield information on available-for-sale securities does not give effect to changes in fair value that are reflected as a component of shareholders' equity. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Table of Contents*Loans Held For Sale*

Loans held for sale totaled \$6 million at December 31, 2007, down 97% from December 31, 2006. The reduction occurred primarily at our home equity line of business where we reclassified \$167 million of mortgage loans held for sale to held for investment during the first quarter reflecting our decision not to sell into weak secondary market conditions. The majority of our new production of home equity product is now either sold within weeks or, is originated for investment. Details related to this reclassification are discussed later in the Home Equity Lending section of this document.

Loans and Leases

Our commercial loans and leases are originated throughout the United States and Canada. At December 31, 2007, 93% of our loan and lease portfolio was associated with our U.S. operations. We also extend credit to consumers throughout the United States through mortgages, installment loans and revolving credit arrangements.

Loans by major category for the periods presented were as follows:

	2007	2006	December 31, 2005	2004	2003
	(Dollars in thousands)				
Commercial, financial and agricultural	\$ 2,099,451	\$ 2,025,890	\$ 1,882,079	\$ 1,643,128	\$ 1,503,619
Real estate construction & land development	586,037	601,699	514,005	334,386	296,180
Real estate mortgage	1,691,450	1,522,616	1,232,933	806,757	856,070
Consumer	32,232	31,581	31,718	31,166	27,370
Commercial financing:					
Franchise financing	925,741	699,969	462,413	330,496	207,341
Domestic leasing	306,301	296,056	237,968	174,035	157,072
Foreign leasing	462,036	358,783	313,581	265,780	207,355
Unearned income:					
Franchise financing	(306,681)	(211,480)	(125,474)	(86,638)	(56,837)
Domestic leasing	(42,723)	(42,782)	(33,267)	(23,924)	(22,038)
Foreign leasing	(57,614)	(44,139)	(38,013)	(34,497)	(29,038)
Total	\$ 5,696,230	\$ 5,238,193	\$ 4,477,943	\$ 3,440,689	\$ 3,147,094

Table of Contents

The following table shows our contractual maturity distribution of loans at December 31, 2007. 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	\$ 579,535	\$ 934,150	\$ 585,766	\$ 2,099,451
Real estate construction & land development	458,184	113,562	14,291	586,037
Real estate mortgage	84,992	158,540	1,447,918	1,691,450
Consumer	14,998	13,750	3,484	32,232
Commercial financing:				
Franchise financing	1,134	86,688	531,238	619,060
Domestic leasing	16,087	247,196	295	263,578
Foreign leasing	23,654	361,423	19,345	404,422
Total	\$ 1,178,584	\$ 1,915,309	\$ 2,602,337	\$ 5,696,230
Loans due after one year with:				
Fixed interest rates				\$ 3,185,833
Variable interest rates				1,331,813
Total				\$ 4,517,646

Allowance for Loan and Lease Losses

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

	December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Balance at beginning of year	\$ 74,468	\$ 59,223	\$ 43,441
Provision for loan and lease losses	134,988	35,101	27,307
Charge-offs	(73,994)	(30,810)	(20,201)
Recoveries	10,099	11,208	8,960
Reduction due to reclassification and sales of loans	(1,225)	(246)	(403)
Foreign currency adjustment	519	(8)	119
Balance at end of period	\$ 144,855	\$ 74,468	\$ 59,223

Increased loan and lease loss provisions and increased charge-offs were experienced across all three of our lines of business in 2007. The majority of the increase occurred at our home equity lending business where we incurred \$103 million of loan loss provision and \$53 million in charge-offs. More information on this subject is contained in

the section on *Credit Risk* and in the line of business discussions.

Deposits

Total deposits in 2007 averaged \$3.4 billion compared to average deposits in 2006 of \$4.0 billion, and average deposits in 2005 of \$3.9 billion. Demand deposits in 2007 averaged \$0.3 billion, down from an average of \$0.8 billion in 2006 and \$1.0 billion in 2005. A significant portion of demand deposits related to deposits associated with escrow accounts held on loans in the servicing portfolio at the discontinued mortgage banking line of business. During 2007, these escrow accounts averaged \$18 million, compared to an average of \$0.4 billion in 2006 and \$0.7 billion in 2005. These escrow accounts were transferred in connection with the transfer of mortgage servicing rights at the mortgage banking line of business.

Table of Contents

Irwin Union Bank and Trust utilizes institutional broker-sourced deposits as funding to supplement deposits solicited through branches and other wholesale funding sources. At December 31, 2007, institutional broker-sourced deposits totaled \$646 million compared to a balance of \$542 million at December 31, 2006.

The following table shows maturities of certificates of deposit (CDs) of \$100,000 or more, brokered deposits, escrows and core deposits at the dates indicated:

	2007	December 31, 2006	2005
	(Dollars in thousands)		
Under 3 months	\$ 350,488	\$ 404,684	\$ 419,574
3 to 6 months	183,001	202,466	230,024
6 to 12 months	79,649	230,561	231,397
after 12 months	48,480	270,070	341,851
Total Certificates of deposit	\$ 661,618	\$ 1,107,781	\$ 1,222,846
Brokered deposits	\$ 646,465	\$ 541,903	\$ 638,007
Mortgage banking escrow deposits	\$ 1,479	\$ 324,913	\$ 412,444
Demand deposits	305,341	362,712	342,913
Money market accounts	1,396,562	1,441,358	1,602,337
Savings and time deposits	636,399	602,703	544,814
Core deposits	\$ 2,338,302	\$ 2,406,773	\$ 2,490,064

Other Borrowings

Other borrowings during 2007 averaged \$599 million compared to an average of \$544 million in 2006, and \$421 million in 2005. Other borrowings increased to \$802 million at December 31, 2007 compared to \$602 million at December 31, 2006. The increase in other borrowings in 2007 related to declining deposit balances in 2007.

The bulk of our other borrowings were in the form of advances from the Federal Home Loan Bank which averaged \$478 million for the year ended December 31, 2007, with an average rate of 5.10%. The balance at December 31, 2007 was \$574 million with an interest rate of 4.97%. The maximum outstanding at any month end during 2007 was \$574 million. At December 31, 2006, Federal Home Loan Bank borrowings averaged \$322 million, with an average rate of 4.90%. The balance at December 31, 2006 was \$372 million at an interest rate of 5.02%. The maximum outstanding at any month end during 2006 was \$609 million.

Collateralized and Other Long-Term Debt

Collateralized debt totaled \$1.2 billion at December 31, 2007, up \$40 million compared to December 31, 2006. The bulk of these borrowings have resulted from securitizations of portfolio loans at the home equity lending line of business that result in loans remaining as assets and debt being accounted for under generally accepted accounting principles (GAAP) on our balance sheet (although to meet the structuring needs of the securitization trusts, the loans

have been legally separated and sold to the trusts). This securitization debt provides us with match-term funding for these loans and leases with the debt being extinguished through pay-downs of the loans.

Other long-term debt totaled \$234 million at December 31, 2007, unchanged from December 31, 2006. We have obligations represented by subordinated debentures totaling \$204 million with our wholly-owned trusts that were created for the purpose of issuing trust preferred securities. The subordinated debentures were the sole assets of the trusts at December 31, 2007 and the sole liabilities were \$198 million of trust preferred securities. In accordance with FASB Interpretation No. 46 (FIN 46), Consolidation of Variable Interest Entities (revised December 2004), we do not consolidate the wholly-owned trusts that issued the trust preferred securities. Instead, the subordinated debentures held by the trusts are disclosed on the balance sheet as other long-term debt. Please refer to the section on Dividends for additional information.

Table of Contents*Capital*

Shareholders' equity averaged \$506 million during 2007, down 4% compared to 2006, and up 5% from 2005. Shareholders' equity balance of \$459 million at December 31, 2007 represented \$15.22 per common share, compared to \$17.30 per common share at December 31, 2006, and compared to \$17.90 per common share at year-end 2005. During 2007, we repurchased \$12.8 million of common stock, compared to \$4.4 million in 2006. We paid an aggregate of \$14.0 million in common dividends during 2007, compared to \$13.1 million during 2006 and \$11.4 million during 2005. We also paid \$1.3 million in preferred dividends in 2007 on our noncumulative perpetual preferred stock.

The following table sets forth our capital and capital ratios at the dates indicated:

	2007	December 31, 2006	2005
	(Dollars in thousands)		
Tier 1 capital	\$ 619,656	\$ 712,403	\$ 675,316
Tier 2 capital	150,212	125,351	154,128
Total risk-based capital	\$ 769,868	\$ 837,754	\$ 829,444
Risk-weighted assets	\$ 6,099,204	\$ 6,258,927	\$ 6,317,797
Risk-based ratios:			
Tier 1 capital	10.2%	11.4%	10.7%
Total capital	12.6	13.4	13.1
Tier 1 leverage ratio	10.2	11.5	10.3
Ending shareholders' equity to assets	7.4	8.5	7.7
Average shareholders' equity to assets	8.3	8.1	8.0

At December 31, 2007, our total risk-based capital ratio was 12.6%, exceeding our internal Policy minimum of 11.0% (we have a higher Policy minimum of 12.0% at our principal subsidiary, Irwin Union Bank and Trust). At December 31, 2006 and 2005, our total risk-based capital ratios were 13.4% and 13.1%, respectively. Our ending equity to assets ratio at December 31, 2007 was 7.4% compared to 8.5% at December 31, 2006. Our Tier 1 capital totaled \$620 million as of December 31, 2007, or 10.2% of risk-weighted assets. For an explanation of capital requirements and categories applicable to financial institutions, see the discussion in this Report under the subsection *Other Safety and Soundness Regulations* in Part 1, Business.

Accumulated other comprehensive income increased by \$5.4 million in 2007, largely reflecting foreign currency adjustments during 2007.

Retained earnings was adjusted at the beginning of 2007 as a result of our adoption of FAS 156 related to accounting for mortgage servicing rights. In accordance with this pronouncement, we recorded as an increase to retained earnings a \$1.7 million one time (tax-affected) cumulative adjustment on January 1, 2007.

In December 2006, we raised \$14 million of floating rate non-cumulative perpetual preferred stock net of issuance costs. This capital is Tier 1 eligible with a five year non-call period, and is callable at par thereafter at our option.

Table of Contents

We have outstanding \$198 million in trust preferred securities as of December 31, 2007. All securities are callable at par after five years from date of issuance. These funds are all Tier 1 qualifying capital under current regulatory guidance. In 2007, \$14 million of dividends were paid related to these securities. On March 3, 2008, we announced the suspension of dividends on these securities. The sole assets of these trusts are our subordinated debentures. See further discussion in the **Other Long-Term Debt** section above. Highlights about these trusts are listed below:

Name	Date	Interest Rate at		Maturity Date	\$ Amount in thousands	Dividend	Other
		Origination	December 31, 2007				
IFC Capital Trust VI	Oct 2002		8.70	Sep 2032	\$ 34,500	quarterly	fixed rate for term
IFC Statutory Trust VII	Nov 2003		7.73	Nov 2033	50,000	quarterly	rate changes quarterly at three month LIBOR plus 290 basis points
IFC Capital Trust VIII	Aug 2005		5.96	Aug 2035	51,750	quarterly	fixed rate for 5 years, variable rate of 3 month LIBOR plus 153 basis points thereafter
IFC Capital Trust IX	Apr 2006		6.69	Apr 2036	31,500	quarterly	fixed rate for 5 years, variable rate of 3 month LIBOR plus 149 basis points thereafter
IFC Capital Trust X	Dec 2006		6.53	Dec 2036	15,000	quarterly	fixed rate for 5 years, variable rate of 3 month LIBOR plus 175 basis points thereafter
IFC Capital Trust XI	Dec 2006		6.89	Mar 2037	15,000	quarterly	floating rate of 3 month LIBOR plus 174 basis
					\$ 197,750		

We have \$30 million of 7.58%, 15-year subordinated debt that is due in 2014, but is callable in 2009 at par. The debt is privately placed. These funds qualify as Tier 2 capital. The securities are not convertible into our common shares.

In order to maintain product price competitiveness with other national banks, we allocate capital to our subsidiaries in a manner which reflects their relative risk and as if they were stand-alone businesses. The allocated amount of capital

varies according to the risk characteristics of the individual business segments and the products they offer. Capital is allocated separately based on the following types of risk: credit, market (including interest rate and foreign currency), liquidity, operational and compliance. We adjust this allocation, as necessary, to assure that we meet regulatory and internal policy standards for minimum capitalization. We utilize internal risk measurement models, and capital requirements from our banking regulators to arrive at the capitalization required by line of business. We re-allocate capital to subsidiaries on a quarterly basis based on their risk and growth plans.

During the third quarter of 2006, our Board authorized management to begin a share repurchase program, contingent on the completion of the sale of the assets of our Discontinued Operations. At the time of the authorization, we believed the sale of the mortgage segment would free-up a significant amount of capital. It was our intention to retain some of that capital for future growth (specifically, reducing the amount we otherwise would have raised to support the growth of our commercial segments) and to use the remainder, up to \$50 million, for share repurchases over several quarters.

We began those repurchases late in the fourth quarter of 2006 and early in 2007. Due to a variety of factors, however, the pace and size of the repurchases were lower than we had anticipated at the time of original authorization. Our exit costs at Irwin Mortgage exceeded our expectations, in large part due to the current weak environment for mortgage banking operations. Second, our risk profile did not decline as much as anticipated due to the remaining risk of loan repurchases in the discontinued segment, the amount of intercompany diversification removed with the sale, and the decision to retain certain mortgage assets in portfolio rather than selling them into a weak market. Third, our earnings, specifically in the home equity sector, were lower than we anticipated during 2007.

Table of Contents

During December of 2006 and the first half 2007, we repurchased shares in this program. However, due to the factors noted above and the constriction of the capital markets in the middle of 2007, we halted our repurchases under this program and are unlikely to be active again in the near- to intermediate-term.

In total, we repurchased 629 thousand shares for \$12.1 million during 2007 in connection with our Board-authorized share repurchase program. Also, in connection with our stock option plans, we repurchased 45 thousand common shares in 2007 with a market value of \$0.7 million. In December of 2006, we repurchased 133 thousand shares for \$3.0 million at the start of our repurchase program. In connection with our stock option plans, we also repurchased 67 thousand common shares in 2006 with a market value of \$1.4 million.

Inflation

Since substantially all of our assets and liabilities are monetary in nature, such as cash, securities, loans and deposits, their values are less sensitive to the effects of inflation than to changes in interest rates. We attempt to control the impact of interest rate fluctuations by managing the relationship between interest rate sensitive assets and liabilities and by hedging certain interest sensitive assets with financial derivatives or forward commitments.

Cash Flow Analysis

Our cash and cash equivalents decreased \$68 million in 2007 compared to a decrease of \$10 million during 2006 and an increase of \$58 million in 2005. The decrease in cash was primarily due to increased loans held for investment, particularly at our commercial finance line of business. Cash flows from operating activities provided \$0.4 billion in cash and cash equivalents in 2007 compared to providing of \$1.1 billion in 2006. The 2007 operating cash was driven by the collection of servicing sale receivables at our discontinued mortgage line of business as well as proceeds on loan sales at our commercial finance line of business.

Earnings by Line of Business

Irwin Financial Corporation is composed of three principal lines of business, the discontinued mortgage banking segment and the parent and other support operations. The three customer-facing segments (lines of business) of continuing operations are:

Commercial Banking

Commercial Finance

Home Equity Lending

The following table summarizes our net income (loss) by line of business for the periods indicated:

	Year Ended December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Net income (loss):			
Commercial Banking	\$ 15,853	\$ 30,860	\$ 27,379
Commercial Finance	13,556	12,600	7,433
Home Equity Lending	(47,451)	1,538	2,252

Edgar Filing: IRWIN FINANCIAL CORP - Form 10-K

Other (including consolidating entries)	(6,088)	(7,597)	(817)
Net income (loss) from continuing operations	(24,130)	37,401	36,247
Discontinued operations	(30,543)	(35,674)	(17,260)
Net income (loss)	\$ (54,673)	\$ 1,727	\$ 18,987

Table of Contents**Commercial Banking**

The following table shows selected financial information for our commercial banking line of business:

	Year Ended December 31,				
	2007	2006	2005	2004	2003
	(Dollars in thousands)				
Selected Income Statement Data:					
Interest income	\$ 232,006	\$ 229,193	\$ 183,052	\$ 127,029	\$ 112,679
Interest expense	(113,077)	(104,467)	(72,294)	(37,412)	(33,663)
Net interest income	118,929	124,726	110,758	89,617	79,016
Provision for loan and lease losses	(18,241)	(5,734)	(5,286)	(3,307)	(5,913)
Other income	16,615	18,173	16,945	18,316	21,070
Total net revenue	117,303	137,165	122,417	104,626	94,173
Operating expense	(92,606)	(88,932)	(77,062)	(65,450)	(56,699)
Income before taxes	24,697	48,233	45,355	39,176	37,474
Income taxes	(8,844)	(17,373)	(17,976)	(15,752)	(14,997)
Net income	\$ 15,853	\$ 30,860	\$ 27,379	\$ 23,424	\$ 22,477
Performance Ratios:					
Return on average equity	6.77%	14.15%	17.38%	15.85%	15.20%
Selected Balance Sheet Data at End of Period:					
Assets	\$ 3,093,764	\$ 3,103,547	\$ 3,162,398	\$ 2,622,877	\$ 2,203,965
Securities and short-term investments	38,780	55,116	340,811 ⁽¹⁾	327,664 ⁽¹⁾	107,668
Loans and leases	2,950,356	2,901,029	2,680,220	2,223,474	1,988,633
Allowance for loan and lease losses	(35,148)	(27,113)	(24,670)	(22,230)	(22,055)
Deposits	2,528,721	2,635,380	2,797,635	2,390,839	1,964,274
Shareholder's equity	235,009	241,556	195,381	143,580	162,050
Daily Averages:					
Assets	\$ 3,143,219	\$ 3,143,439	\$ 3,025,717	\$ 2,476,835	\$ 2,119,944
Loans and leases	2,902,994	2,797,853	2,460,560	2,094,190	1,914,608
Allowance for loan and lease losses	(26,984)	(26,175)	(23,656)	(22,304)	(21,895)
Deposits	2,753,615	2,826,446	2,766,289	2,258,538	1,894,406
Shareholder's equity	234,068	218,076	157,545	147,759	147,886
Shareholder's equity to assets	7.45%	6.95%	5.21%	5.97%	6.98%

- (1) Includes \$317 million and \$293 million of inter-company investments in 2005 and 2004, respectively, the result of excess liquidity at the commercial banking line of business related to deposit growth in excess of its asset deployment needs. The funds were redeployed in earning assets at our other lines of business.

Overview

Our commercial banking line of business focuses on providing credit, cash management and personal banking products 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.

Table of Contents*Commercial Banking Strategy*

Our strategy in commercial banking focuses on providing personalized banking services to small businesses and their owners, using personal relationship and non-conventional means of creating convenience to add value. We specialize in developing added value relationships through the ability to customize products, services and advice based on exceptional and experienced team members who develop in-depth knowledge of our customers and their businesses. We offer banking, insurance, and investment products to provide a full range of financial services to our small business customers. We seek to redefine convenience in serving both small business customers in a metro area and consumers in the neighborhoods of our branches by leveraging technology, couriers and personal service to bring the bank to you. We do this in markets selected on the basis of the attractiveness of their small business communities, competitive conditions and the availability of experienced and exceptional bankers to join our team.

We expect consolidation to continue in the banking and financial services industry both in our existing markets and in those we do not serve. Long-term, we plan to capitalize on the opportunities brought about in this environment by continuing the bank's growth strategy for small business banking in existing markets and in new markets throughout the United States. Our focus will be to provide personalized banking services to small businesses, using experienced local staff with a strong presence in cities affected by the industry-wide consolidations and possessing attractive small business environments. Our expansion into new markets is subject to regulatory approval.

Portfolio Characteristics

The following tables show the geographic composition of our commercial banking loans and our core deposits:

Markets	2007			December 31, 2006			2005		
	Loans	Percent	Weighted	Loans	Percent	Weighted	Loans	Percent	Weighted
	Outstanding	of Total	Average Yield	Outstanding (Dollars in thousands)	Total	Average Yield	Outstanding	of Total	Average Yield
Indianapolis Central and Western Michigan Southern Indiana Phoenix Las Vegas Other	\$ 539,008 465,924 463,597 484,985 188,126 808,716	18.3% 15.8 15.7 16.4 6.4 27.4	7.1% 7.3 6.7 7.0 8.2 7.5	\$ 561,343 519,348 475,051 452,919 154,218 738,150	19.3% 17.9 16.4 15.6 5.3 25.5	7.6% 7.7 7.2 7.9 8.1 7.9	\$ 560,775 516,444 454,236 447,548 112,761 588,456	20.9% 19.3 16.9 16.7 4.2 22.0	7.0% 7.1 6.5 7.6 7.5 7.2
Total	\$ 2,950,356	100.0%	7.3%	\$ 2,901,029	100.0	7.7%	\$ 2,680,220	100.0	7.1%

Markets	2007			December 31, 2006			2005		
	Core	Percent	Weighted	Core	Percent	Weighted	Core	Percent	Weighted
	Deposits	of Total	Average Yield	Deposits	Total	Average Yield	Deposits	of Total	Average Yield
Indianapolis Central and Western Michigan Southern Indiana Phoenix Las Vegas Other	\$ 539,008 465,924 463,597 484,985 188,126 808,716	18.3% 15.8 15.7 16.4 6.4 27.4	7.1% 7.3 6.7 7.0 8.2 7.5	\$ 561,343 519,348 475,051 452,919 154,218 738,150	19.3% 17.9 16.4 15.6 5.3 25.5	7.6% 7.7 7.2 7.9 8.1 7.9	\$ 560,775 516,444 454,236 447,548 112,761 588,456	20.9% 19.3 16.9 16.7 4.2 22.0	7.0% 7.1 6.5 7.6 7.5 7.2
Total	\$ 2,950,356	100.0%	7.3%	\$ 2,901,029	100.0	7.7%	\$ 2,680,220	100.0	7.1%

Edgar Filing: IRWIN FINANCIAL CORP - Form 10-K

(Dollars in thousands)

Indianapolis	\$	225,075	10.0%	3.5%	\$	259,835	10.8%	2.4%	\$	259,196	10.4%	2.1%
Central and Western												
Michigan		195,818	8.7	2.6		231,666	9.7	3.4		238,742	9.6	2.6
Southern Indiana		740,686	33.1	2.9		630,060	26.3	2.8		674,923	27.1	2.1
Phoenix		175,617	7.8	3.4		179,502	7.5	3.4		190,428	7.6	2.4
Las Vegas		429,693	19.2	3.7		467,708	19.5	4.1		413,541	16.6	3.5
Other		473,827	21.2	3.2		631,268	26.2	3.5		713,233	28.7	3.3
Total	\$	2,240,716	100.0%	3.1%	\$	2,400,039	100.0%	3.3%	\$	2,490,063	100.0%	2.7%

Table of Contents*Net Income*

Commercial banking net income decreased to \$16 million during 2007, down 49%, compared to \$31 million in 2006, and down 42% compared to 2005 net income of \$27 million. The 2007 decline in earnings relates to higher loan loss provision and lower net interest income .

Net Interest Income

The following table shows information about net interest income for our commercial banking line of business:

	Year Ended December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Net interest income	\$ 118,929	\$ 124,726	\$ 110,758
Average interest earning assets	3,040,560	3,028,527	2,914,352
Net interest margin	3.91%	4.12%	3.80%

Net interest income was \$119 million, a decrease of 5% over 2006, and an increase of 7% from 2005. The 2007 decline in net interest income resulted primarily from a change in mix of liabilities toward higher cost deposits as well as a shift in mix of our loan portfolio from higher rate adjustable loans to lower fixed rate loans resulting from the inverted yield curve that has been prevalent over the time periods compared. Net interest margin is computed by dividing net interest income by average interest earning assets. Net interest margin during 2007 was 3.91%, compared to 4.12% in 2006, and 3.80% in 2005. The decline in 2007 margin reflects competitive conditions, product mix, and unfavorable repricing of loans and deposits.

Provision for Loan and Lease Losses

Provision for loan and lease losses was \$18.2 million in 2007, compared to provisions of \$5.7 million and \$5.3 million in 2006 and 2005, respectively. The increased provision relates to weakening credit quality, particularly commercial real estate credits in connection with the residential housing markets, both in the Midwest and Western markets. Approximately one-third of the increased provision relates to a loss identified in the first quarter related to a commercial credit in Michigan. With respect to this credit, we believe the borrower will be unable to repay the majority of the loan as we discovered what we believe were misrepresentations about collateral offered for the loan. As such, we took a charge-off of \$4.2 million related specifically to this loan during 2007. See further discussion in Credit Quality section later in this document.

Noninterest Income

The following table shows the components of noninterest income for our commercial banking line of business:

	Year Ended December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Service charges on deposit accounts	\$ 3,865	\$ 4,307	\$ 4,008
Gain from sales of loans	1,931	2,328	2,943

Edgar Filing: IRWIN FINANCIAL CORP - Form 10-K

Trust fees	2,307	1,971	1,964
Insurance commissions, fees and premiums	1,812	1,955	1,827
Brokerage fees	1,623	1,369	1,452
Loan servicing fees	1,462	1,523	1,473
Amortization and recovery of servicing assets	(1,084)	(1,140)	(1,058)
Other	4,699	5,860	4,336
Total noninterest income	\$ 16,615	\$ 18,173	\$ 16,945

Table of Contents

Noninterest income during 2007 decreased 9% over 2006 and decreased 2% over 2005. The 2007 decrease was due primarily to lower service charges on deposit accounts, lower gains on sales of loans, and to a loss on sale of other real estate owned (OREO).

Operating Expenses

The following table shows the components of operating expenses for our commercial banking line of business:

	Year Ended December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Salaries and employee benefits	\$ 51,374	\$ 53,111	\$ 47,934
Other expenses	41,232	35,821	29,128
Total operating expenses	\$ 92,606	\$ 88,932	\$ 77,062
Efficiency ratio	68.3%	62.2%	60.3%
Number of employees at period end ⁽¹⁾	532	585	586

⁽¹⁾ On a full time equivalent basis

Operating expenses during 2007 totaled \$93 million, an increase of 4% over 2006, and an increase of 20% from 2005. The increase in operating expenses in 2007 is primarily related to investments in risk management systems and upgrades of technologies. Our level of operating expenses was too high in 2007 relative to our revenue generation and led to a staff reduction in the fourth quarter to achieve better alignment.

Balance Sheet

Total assets for the year ended December 31, 2007 averaged \$3.1 billion, relatively unchanged from 2006 and up from \$3.0 billion in 2005. Average earning assets for the year ended December 31, 2007 were \$3.0 billion, again relatively unchanged from 2006, and up from \$2.9 billion in 2005. Average core deposits for the year totaled \$2.3 billion, a decrease of 1% over average core deposits in 2006, and an increase of 6% from 2005.

Table of Contents*Credit Quality*

Our credit quality declined in 2007, reflecting trends in the regional economies in which we participate. As a result, the allowance for loan losses to total loans increased to 1.19% at December 31, 2007, compared to 0.93% at December 31, 2006. Total nonperforming assets increased \$15.0 million in 2007 versus 2006. Other real estate owned (OREO) increased \$2.5 million compared to the 2006 balance. While our nonperforming loans are not significantly concentrated in any market, a greater than average amount of our nonperforming loans are located in our Michigan market. Many of the nonperforming loans relate to commercial real estate credits impacted by the deteriorating residential housing markets, both in the Midwest and Western markets. We have seen an increase in charge-offs in 2007 compared to 2006, directionally consistent with the increase in allowance as a percent of total loans. The following table shows information about our nonperforming assets in this line of business and our allowance for loan losses.

	2007	December 31, 2006	2005
	(Dollars in thousands)		
Nonperforming loans	\$ 27,001	\$ 14,455	\$ 19,483
Other real estate owned	6,895	4,423	7,892
Total nonperforming assets	\$ 33,896	\$ 18,878	\$ 27,375
Nonperforming assets to total assets	1.09%	0.61%	0.87%
Allowance for loan losses	\$ 35,148	\$ 27,113	\$ 24,670
Allowance for loan losses to total loans	1.19%	0.93%	0.92%
For the Period Ended:			
Provision for loan losses	\$ 18,241	\$ 5,734	\$ 5,286
Net charge-offs	10,206	3,291	2,847
Net charge-offs to average loans	0.35%	0.13%	0.12%

The following table shows the ratio of nonperforming assets to total loans for select markets for the periods indicated:

Markets	2007	December 31, 2006	2005
Indianapolis	1.02%	0.24%	0.58%
Central and Western Michigan	2.52	2.72	3.76
Southern Indiana	0.53	0.14	0.24
Phoenix	1.20	0.52	0.60
Las Vegas	0.01		
Other ⁽¹⁾	1.03	0.06	0.16
Total	1.15%	0.65%	1.02%

(1) 89% of Other in 2007 relates to a single credit in the Sacramento market where our portfolio totals \$120 million

Table of Contents**Commercial Finance**

	Year Ended December 31,				
	2007	2006	2005	2004	2003
	(Dollars in thousands)				
Selected Income Statement Data:					
Net interest income	\$ 52,721	\$ 42,545	\$ 33,683	\$ 28,084	\$ 22,766
Provision for loan and lease losses	(13,505)	(6,701)	(6,211)	(6,798)	(11,308)
Noninterest income	13,106	8,018	7,437	6,275	5,868
Total net revenue	52,322	43,862	34,909	27,561	17,326
Operating expense	(30,107)	(23,955)	(22,224)	(18,782)	(15,072)
Income before taxes	22,215	19,907	12,685	8,779	2,254
Income taxes	(8,659)	(7,307)	(5,252)	(5,562)	(461)
Net income	\$ 13,556	\$ 12,600	\$ 7,433	\$ 3,217	\$ 1,793
Selected Balance Sheet Data at End of Period:					
Total assets	\$ 1,302,688	\$ 1,073,552	\$ 831,657	\$ 636,604	\$ 474,915
Loans and leases	1,287,060	1,056,406	817,208	625,140	463,423
Allowance for loan and lease losses	(17,792)	(13,525)	(10,756)	(9,624)	(11,445)
Shareholder's equity	119,574	88,587	71,568	55,993	44,255
Selected Operating Data:					
Net charge-offs	\$ 8,533	\$ 3,678	\$ 4,806	\$ 8,235	\$ 7,868
Net interest margin	4.58%	4.55%	4.80%	5.33%	5.63%
Total funding of loans and leases	\$ 700,718	\$ 595,319	\$ 451,524	\$ 366,545	\$ 272,685
Return on average equity	12.70%	17.44%	13.70%	7.70%	5.60%

Overview

We established this line of business in 1999. We offer commercial finance products and services through a direct subsidiary of our banking subsidiary, Irwin Union Bank and Trust, an Indiana state-chartered commercial bank and its direct and indirect subsidiaries. In this segment, we provide small ticket lease financing on a variety of small business equipment in the United States and Canada as well as equipment and leasehold improvement financing for franchisees (mainly in the quick service restaurant sector) in the United States. In 2006, we expanded our product line to include professional practice financing and information technology leasing to middle and upper middle market companies throughout the United States and Canada.

Commercial Finance Strategy

We provide financing alternatives to small businesses generally and to franchisees. We utilize direct and indirect sales forces to distribute our products. In the small ticket lease channel, our sales efforts focus on providing lease solutions

for vendors and manufacturers. The average lease size is approximately \$30 thousand. The majority of our leases are full payout (no residual), small-ticket assets secured by commercial equipment. We finance a variety of commercial, light industrial and office equipment. Within the franchise channel, the financing of equipment and real estate is structured as loans. The loan amounts average approximately \$500 thousand.

Table of Contents*Portfolio Characteristics*

The following table shows the geographic composition of our commercial finance loans and leases at the dates shown:

	December 31,	
	2007	2006
United States		
California	11.5%	12.4%
Texas	8.0	5.9
New York	4.7	5.0
Florida	4.3	4.0
All other states	40.1	42.8
Total United States	68.6%	70.1%
Canada⁽¹⁾		
Ontario	7.5%	7.3%
Quebec	7.2	7.1
British Columbia	7.2	7.0
Alberta	6.5	5.8
All other provinces	3.0	2.7
Total Canada	31.4%	29.9%
Total North America	100.0%	100.0%
Total Portfolio in thousands	\$ 1,287,060	\$ 1,056,406

(1) in U.S. dollars

The following table provides yield and delinquency information about the loan and lease portfolio of our commercial finance line of business at the dates shown:

	December 31,	
	2007	2006
	(Dollars in thousands)	
Domestic franchise loans	\$ 619,060	\$ 488,489
Weighted average coupon	9.38%	8.79%
Delinquency ratio	0.04	0.16
Domestic leases	\$ 263,578	\$ 253,274
Weighted average coupon	10.91%	10.32%
Delinquency ratio	2.47	1.72
Canadian leases ⁽¹⁾	\$ 404,422	\$ 314,644
Weighted average coupon	9.09%	9.13%
Delinquency ratio	0.51	0.36

(1) in U.S. dollars

Net Income

Commercial finance net income increased to \$14 million during 2007, a 8% increase compared to net income of \$13 million during 2006. In 2005, net income totaled \$7 million. Results in 2007 reflect growth of \$10 million in net interest income over 2006. Net interest income in 2007 increased 57% over 2005. Provision for loan and lease losses increased to \$13.5 million in 2007, compared to provisions of \$6.7 million and \$6.2 million in 2006 and 2005,

Table of Contents

respectively. The 2007 earnings growth is attributable to higher net interest income due to portfolio growth and to a 63% increase in noninterest revenue primarily related to higher gains on sales of loans.

Net Interest Income

The following table shows information about net interest income for our commercial finance line of business:

	Year Ended December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Net interest income	\$ 52,721	\$ 42,545	\$ 33,683
Average interest earning assets	1,151,470	936,519	701,423
Net interest margin	4.58%	4.55%	4.80%

Net interest income was \$53 million for 2007, an increase of 24% over 2006, and an increase of 57% from 2005. The improvement in net interest income resulted from an increase in our commercial finance portfolio. The total loan and lease portfolio has increased to \$1.3 billion at December 31, 2007, an increase of 22% and 57% over year-end 2006 and 2005 balances, respectively. This line of business originated \$701 million in loans and leases during 2007, compared to \$595 million during 2006 and \$452 million in 2005. The portfolio increased \$53 million as of December 31, 2007 relative to December 31, 2006 due solely to the increased value of the Canadian dollar relative to the U.S. dollar.

Net interest margin during 2007 was 4.58%, compared to 4.55% in 2006, and 4.80% in 2005. The increased margin in 2007 is due primarily to product mix.

Provision for Loan and Lease Losses

The provision for loan and lease losses increased to \$13.5 million in 2007 compared to \$6.7 million in 2006 and \$6.2 million in 2005. The increased provisioning levels in 2007 relate to growth in our loan and lease portfolio as well as some credit deterioration in our small ticket lease portfolio. See **Credit Quality** section below for further discussion.

Noninterest Income

The following table shows the components of noninterest income for our commercial finance line of business:

	Year Ended December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Gain from sales of loans	\$ 6,779	\$ 2,563	\$ 2,642
Derivative losses, net	(547)	(263)	(717)
Other	6,874	5,718	5,512
Total noninterest income	\$ 13,106	\$ 8,018	\$ 7,437

Noninterest income during 2007 increased 63% over 2006 and 76% over 2005. Included in noninterest income were gains that totaled \$6.8 million in 2007 compared to \$2.6 million in both 2006 and 2005. The 2007 gains include \$4.4 million in gains on whole loan sales of \$79 million. In addition, the 2007 gains include gains of \$2.4 million related to \$65 million of participations sold during the year from our franchise loan portfolio. We had no loan participation sales in 2006 or 2005. Also included in noninterest income during 2007, 2006 and 2005 was \$0.5 million, \$0.3 million and \$0.7 million, respectively, of interest rate derivative mark to market valuation losses in our Canadian operation related to managing interest rate risk exposure in our funding of that operation. Other noninterest revenue is up 20% over 2006 due in part to higher gains on sales of end of term leased property.

Table of Contents*Operating Expenses*

The following table shows the components of operating expenses for our commercial finance line of business:

	Year Ended December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Salaries and employee benefits	\$ 18,441	\$ 13,155	\$ 11,306
Other	11,666	10,800	10,918
Total operating expenses	\$ 30,107	\$ 23,955	\$ 22,224
Efficiency ratio	45.7%	47.4%	54.0%
Number of employees at period end ⁽¹⁾	215	202	184

(1) On a full time equivalent basis

Operating expenses during 2007 totaled \$30 million, an increase of 26% over 2006, and an increase of 35% from 2005. The increased operating expenses relate to the continued growth in this business, including compensation costs related to higher production levels, infrastructure and staffing development, as well as incentive compensation costs related to profitability.

Credit Quality

The commercial finance line of business had nonperforming loans and leases at December 31, 2007 totaling \$8.9 million, compared to non-performing loans and leases at December 31, 2006 and 2005 totaling \$5.4 million and \$3.7 million, respectively. Net charge-offs recorded by this line of business totaled \$8.5 million in 2007 compared to \$3.7 million in 2006 and \$4.8 million in 2005. The increases in non-performing assets and charge-offs were principally concentrated in our U.S. small ticket portfolio.

Allowance for loan and lease losses at December 31, 2007 totaled \$17.8 million, representing 1.38% of loans and leases, compared to a balance at December 31, 2006 of \$13.5 million, representing 1.28% of loans and leases and a balance of \$10.8 million or 1.32% of the portfolio at December 31, 2005. The increase in loan loss provision is directionally consistent with the increase in charge-offs as indicated below.

Table of Contents

The following table shows information about our nonperforming loans and leases in this line of business and our allowance for loan and lease losses:

	2007	December 31, 2006	2005
	(Dollars in thousands)		
Small Ticket Leases:			
Nonperforming leases	\$ 5,246	\$ 4,583	\$ 2,980
Repossessed Inventory	1,242	664	804
Allowance for lease losses	11,831	7,756	6,638
Allowance for lease losses to total leases	1.77%	1.37%	1.38%
For the Period Ended:			
Provision for lease losses	\$ 10,938	\$ 4,103	\$ 4,585
Net charge-offs	7,440	3,233	3,961
Net charge-offs to average leases	1.20%	0.60%	0.93%
Franchise Loans:			
Nonperforming loans	\$ 3,630	\$ 791	\$ 720
Allowance for loan losses	5,961	5,769	4,118
Allowance for loan losses to total loans	0.96%	1.18%	1.22%
For the Period Ended:			
Provision for loan losses	\$ 2,567	\$ 2,598	\$ 1,626
Net charge-offs	1,093	445	845
Net charge-offs to average loans	0.21%	0.11%	0.30%

Table of Contents**Home Equity Lending**

The following table shows selected financial information for the home equity lending line of business:

	Year Ended December 31,				
	2007	2006	2005	2004	2003
	(Dollars in thousands)				
Selected Income Statement					
Data:					
Net interest income	\$ 95,095	\$ 96,068	\$ 88,290	\$ 98,983	\$ 106,545
Provision for loan and lease losses	(103,242)	(22,659)	(15,811)	(4,369)	(29,575)
Noninterest income	2,535	15,186	33,667	67,847	(19,525)
Total net revenues	(5,612)	88,595	106,146	162,461	57,445
Operating expenses	(73,432)	(85,967)	(102,339)	(114,779)	(90,538)
(Loss) income before taxes	(79,044)	2,628	3,807	47,682	(33,093)
Income taxes	31,593	(1,090)	(1,555)	(19,615)	13,203
Net (loss) income	\$ (47,451)	\$ 1,538	\$ 2,252	\$ 28,067	\$ (19,890)
Selected Balance Sheet					
Data:					
Total assets	\$ 1,481,306	\$ 1,617,219	\$ 1,602,400	\$ 992,979	\$ 1,070,634
Home equity loans and lines of credit ⁽¹⁾	1,458,564	1,280,497	980,406	590,175	692,637
Allowance for loan losses	(91,700)	(33,614)	(23,552)	(11,330)	(29,251)
Home equity loans held for sale	5,865	236,636	513,231	227,740	202,627
Residual interests	3,120	2,760	15,580	51,542	70,519
Mortgage servicing assets	20,071	28,231	30,502	44,000	28,425
Other borrowings	291,293	446,163	920,636	359,902	368,640
Collateralized debt	970,733	948,939	452,615	352,625	460,535
Shareholder's equity	156,894	155,791	151,677	136,260	128,555
Selected Operating Data:					
Loan volume:					
Lines of credit	\$ 33,106	\$ 150,306	\$ 436,451	\$ 508,287	\$ 324,094
Loans	421,838	853,527	1,255,185	934,027	809,222
Total managed portfolio balance	1,605,032	1,708,975	1,593,509	1,147,137	1,513,289
Delinquency ratio ⁽²⁾	5.8%	3.2%	3.0%	4.8%	5.9%
Total managed portfolio balance including credit risk sold	\$ 2,377,464	\$ 2,853,726	\$ 3,058,842	\$ 2,807,367	\$ 2,568,356
Weighted average coupon rate:					

Edgar Filing: IRWIN FINANCIAL CORP - Form 10-K

Lines of credit	10.62%	11.13%	10.17%	9.18%	9.71%
Loans	11.07	10.75	10.18	11.87	12.07
Gain on sale of loans to loans sold	0.51	1.32	2.51	2.24	3.81
Net home equity charge-offs to average managed portfolio	3.24	1.00	0.60	2.48	4.37

(1) Includes \$1.1 billion, \$1.1 billion, \$0.5 billion, \$0.4 billion and \$0.5 billion of loans at December 31, 2007, 2006, 2005, 2004, and 2003, respectively, that collateralize securitized financings.

(2) Nonaccrual loans are included in the delinquency ratio.

Table of Contents*Overview*

Our home equity lending line of business originates, purchases, sells, and services a variety of mortgage loans nationwide. We offer mortgage products through our banking subsidiary, Irwin Union Bank and Trust, an Indiana state-chartered commercial bank and its direct subsidiary. We market our first mortgage and home equity offering principally through mortgage brokers and correspondent lenders, and also directly to consumers. Our target customers are creditworthy homeowners with limited equity in their homes as well as lenders/third parties that can benefit from specialized servicing.

Strategy

We offer mortgage loans with high combined loan-to-value (CLTV) ratios to borrowers we believe have prime credit-quality. Prior to February of 2008, we offered home equity loans with CLTVs up to 125% of their collateral value. In February 2008, we announced that we are halting production of all loans with a CLTV greater than 95% of collateral value. Mortgage loans are priced using a proprietary model, taking into account, among other factors, the credit history of our customer and the relative loan-to-value (LTV) ratio of the loan at origination. Historically, we sold loans through whole loan sales or funded these loans on balance sheet through secured, term financings.

In the second half of 2007, the secured, term funding market closed down. As a result, we significantly narrowed our underwriting guidelines, reduced production staff, and limited our production to only those second mortgage loans we wished to retain on balance sheet or first mortgage loans we could sell to correspondents. Market conditions in late 2007 and early 2008 are such that the current level of originations are materially reduced from our traditional levels.

In an effort to manage portfolio concentration risk and to comply with existing banking regulations, we have policies in place governing the size of our investment in loans secured by real estate where the LTV is greater than 90%. For most of our home equity product offerings, we offer customers the choice to accept an early repayment fee in exchange for a lower interest rate.

Geographic Distribution of our Portfolio and Current Originations

Portfolio: The following table shows the geographic composition of our home equity lending managed portfolio on a percentage basis as of December 31, 2007 and December 31, 2006:

State	December 31,	
	2007	2006
California	9.8%	10.2%
Michigan	7.9	7.8
Colorado	7.6	7.0
Ohio	6.7	6.2
Florida	6.3	7.8
All other states	61.7	61.0
Total	100.0%	100.0%
Total managed portfolio in thousands	\$ 1,605,032	\$ 1,708,975

Table of Contents

Originations: The following table shows the geographic composition of our home equity loan originations on a percentage basis for the periods indicated:

State	December 31,	
	2007	2006
California	9.4%	8.3%
Colorado	7.9	6.5
Pennsylvania	5.7	4.0
Florida	5.1	14.0
Missouri	5.1	2.1
All other states	66.8	65.1
Total	100.0%	100.0%

For the year ended December 31, 2007, loans with loan-to-value ratios greater than 100%, but less than 125% (high LTVs, or HLTVs) constituted 51% of our loan originations and 55% of our managed portfolio for this line of business. HLTVs constituted 47% of our managed portfolio at December 31, 2006. Approximately 68%, or \$1.1 billion, of our home equity managed portfolio at December 31, 2007 was originated with early repayment provisions. The following table provides a breakdown of our home equity lending managed portfolio by product type, outstanding principal balance and weighted average coupon as of December 31, 2007 and 2006:

	December 31, 2007			December 31, 2006		
	Amount	% of Total	Weighted Average Coupon (Dollars in thousands)	Amount	% of Total	Weighted Average Coupon
Home Equity Portfolio						
Loans 100% CLTV	\$ 425,939	26.54%	9.04%	\$ 536,387	31.39%	9.10%
Lines of credit 100% CLTV	246,524	15.36	9.35	319,415	18.69	9.96
First mortgages 100% CLTV	49,962	3.11	7.68	44,727	2.62	7.37
Total 100% CLTV	722,425	45.01	9.05	900,529	52.70	9.32
Loans > 100% CLTV	766,168	47.74	12.50	677,119	39.62	12.36
Lines of credit > 100% CLTV	87,825	5.47	14.00	101,683	5.95	14.55
First mortgages > 100% CLTV	23,584	1.47	8.48	22,916	1.34	8.48
Total > 100% CLTV	877,577	54.68	12.54	801,718	46.91	12.53
Other	5,030	0.31	13.58	6,728	0.39	15.03

Total managed portfolio ⁽¹⁾	\$ 1,605,032	100.00%	10.97%	\$ 1,708,975	100.00%	10.85%
--	--------------	---------	--------	--------------	---------	--------

(1) We define our Managed Portfolio as the portfolio of loans (\$1.6 billion) that we service and on which we carry credit risk. At December 31, 2007, we also serviced another \$0.8 billion of loans for which the credit risk is held by others.

Table of Contents

The following table shows the composition of our loan volume by categories for the periods indicated:

Product	Year Ended December 31,	
	2007	2006
	(Funding amount in thousands)	
First mortgage loans		
Funding Amount	\$ 106,103	\$ 76,499
Weighted Average Disposable Income	5,348	4,944
Weighted Average FICO score	698	689
Weighted Average Coupon	8.29%	8.24%
First mortgage loans up to 110%		
Funding Amount	\$ 2,427	\$ 23,163
Weighted Average Disposable Income	4,059	5,886
Weighted Average FICO score	710	707
Weighted Average Coupon	9.09%	8.50%
Home equity loans up to 100% CLTV		
Funding Amount	\$ 97,788	\$ 440,207
Weighted Average Disposable Income	5,527	6,238
Weighted Average FICO score	699	703
Weighted Average Coupon	10.36%	10.87%
Home equity loans up to 125% CLTV		
Funding Amount	\$ 215,520	\$ 313,658
Weighted Average Disposable Income	4,807	4,382
Weighted Average FICO score	699	698
Weighted Average Coupon	12.95%	12.55%
Home equity lines of credit up to 100% CLTV		
Funding Amount	\$ 16,877	\$ 134,574
Weighted Average Disposable Income	6,532	6,272
Weighted Average FICO score	695	693
Weighted Average Coupon	10.99%	9.67%
Home equity lines of credit up to 125% CLTV		
Funding Amount	\$ 16,228	\$ 15,732
Weighted Average Disposable Income	5,332	4,988
Weighted Average FICO score	696	690
Weighted Average Coupon	15.06%	15.08%
All Products		
Funding Amount	\$ 454,944	\$ 1,003,833
Weighted Average Disposable Income	5,164	5,389
Weighted Average FICO score	698	699

Weighted Average Coupon	11.29%	11.04%
-------------------------	--------	--------

Net Income

Our home equity lending business recorded a net loss of \$47.5 million during the year ended December 31, 2007, compared to net income of \$1.5 million in 2006 and \$2.3 million in 2005.

Table of Contents*Net Revenue*

Net revenue in 2007 totaled \$(6) million, compared to net revenue in 2006 and 2005 of \$89 million and \$106 million, respectively. The decline in net revenues is primarily a result of higher provision for loan losses which is discussed in greater detail in the Home Equity Servicing Credit Quality section below.

Our home equity lending business produced \$0.5 billion of home equity loans in 2007 compared to \$1.0 billion in 2006 and \$1.7 billion in 2005. The decline in loan production in 2007 is a result of tightening guidelines and significantly reduced demand in the secondary market. The production decline accelerated during the second half of the year. In the fourth quarter of 2007, we originated only \$39 million of new loans. The table below shows our originations by channel for the periods shown. Other principally included loans originated in a co-marketing alliance with our now discontinued mortgage banking segment.

	Year Ended December 31,	
	2007	2006
Total originations in thousands	\$ 454,944	\$ 1,003,833
Percent correspondent	35%	27%
Percent retail loans	8	16
Percent brokered	55	32
Percent other	2	25

The following table sets forth certain information regarding net revenue for the periods indicated:

	Year Ended December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Net interest income	\$ 95,095	\$ 96,068	\$ 88,290
Provision for loan losses	(103,242)	(22,659)	(15,811)
Gain on sale of whole loans	950	5,048	18,767
Gain (loss) on intercompany transactions	2,091	866	(210)
Valuation adjustment on loans held for sale	(8,194)	(8,300)	(708)
(Loss) gain on sales of loans	(5,153)	(2,386)	17,849
Loan servicing fees	17,813	31,322	38,206
Amortization of servicing assets	(115)	(19,887)	(29,708)
(Impairment) recovery of servicing assets	(10,946)	647	643
Derivative (losses) gains	(350)	3,136	1,367
Other income	1,286	2,354	5,310
Total net revenue	\$ (5,612)	\$ 88,595	\$ 106,146

Net interest income was \$95 million in 2007, down slightly from 2006 net interest income of \$96 million, and up from \$88 million in 2005.

Provision for loan losses increased to \$103 million in 2007 compared to \$23 million in 2006 and \$16 million in 2005. The increase in provision reflects declining credit quality of home equity loans throughout 2007. During the fourth quarter, the actual and expected performance of portfolio loans continued to deteriorate, leading to the need to provide additional reserves for probable loan losses. We expect weakness in this portfolio to continue as long as challenging conditions in the mortgage market persist.

We completed whole loan sales during 2007 totaling \$0.2 billion resulting in a gain on sale of loans of \$1 million, compared to \$5 million in gain on the sales of \$0.4 billion of loans during 2006. In addition, net charge-offs on our loans held for sale portfolio reduced the gain on sale during 2007 and 2006.

Loan servicing fees totaled \$18 million in 2007 compared to \$31 million in 2006 and \$38 million in 2005. The servicing portfolio on which we earn separately recorded servicing fees at our home equity lending line of business

Table of Contents

totaled \$0.9 billion and \$1.3 billion at December 31, 2007 and 2006, respectively. This is a subset of our entire servicing portfolio. The remainder of the servicing portfolio is associated with loans financed with securitizations, but accounted for under GAAP as portfolio loans. The decrease in loan servicing fees in 2007 relates to the smaller servicing portfolio.

Included in loan servicing fees are incentive servicing fees (ISFs). As part of certain whole loan sales, we have the right to an incentive servicing fee that will provide cash payments to us once a pre-established return for the certificate holders and certain structure-specific loan credit and servicing performance metrics are met. At December 31, 2007, we were receiving incentive fees for six transactions that met these performance metrics. During 2007, we earned \$6.0 million in ISF fees, compared to \$9.1 million during 2006. The following table summarizes ISF revenue recognized by quarter:

	2007	2006	2005
	(Dollars in thousands)		
First Quarter	\$ 1,933	\$ 1,387	\$ 325
Second Quarter	1,708	4,278	681
Third Quarter	1,424	659	851
Fourth Quarter	939	2,757	481
Year to date	\$ 6,004	\$ 9,081	\$ 2,338

Amortization and impairment of servicing assets includes amortization expenses and valuation adjustments relating to the carrying value of servicing assets. We determine fair value of the home equity lending servicing assets using discounted cash flows and assumptions as to estimated future servicing income and costs that we believe market participants would use to value similar assets. In addition, we periodically assess these modeled assumptions for reasonableness through independent third-party valuations. At December 31, 2007, net servicing assets totaled \$20 million, compared to a balance of \$28 million at December 31, 2006, and \$31 million at December 31, 2005. Servicing asset amortization expense, net of impairment, totaled \$11 million during 2007, compared to \$19 million in 2006, and \$29 million in 2005. The 2007 decrease is a result of the decline in the size of the underlying servicing portfolio and slower prepayment speeds. During the first quarter of 2007, the home equity lending line of business adopted the fair value method of accounting for mortgage servicing rights in accordance with SFAS 156. As a result, we are no longer amortizing servicing rights underlying high loan-to-value first mortgages and second mortgages. Rather, we are adjusting the fair value each quarter and recognizing a fair value adjustment through impairment on the income statement.

We originate fixed rate loans that are susceptible to decreases in value in a period of increasing interest rates. We sell loans structured as secured financings (see Footnotes 11 and 15). This type of structure results in cash being received and debt recorded. For certain segments of these transactions there may be fixed rate loans financed by floating interest rate debt. Increasing interest rates could result in a decrease in the net interest rate margin. To protect against such decreases, we enter into derivative contracts. These contracts resulted in a \$0.4 million loss in 2007. This compares to derivative gains of \$3.1 million and \$1.4 million in 2006 and 2005, respectively.

Operating Expenses

The following table shows operating expenses for our home equity lending line of business for the periods indicated:

	Year Ended December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Salaries and employee benefits	\$ 44,528	\$ 51,335	\$ 64,432
Other	28,904	34,632	37,907
Total operating expenses	\$ 73,432	\$ 85,967	\$ 102,339
Number of employees at period end ⁽¹⁾	340	492	615

⁽¹⁾ On a full time equivalent basis.

Table of Contents

Operating expenses were \$73 million for the year ended December 31, 2007, down from \$86 million in 2006, and a decrease of 28% from 2005. Operating expenses declined in 2007 primarily due to restructuring and downsizing over the past two years as well as other cost cutting initiatives. Our 2007 operating expenses included severance and restructuring charges of \$5 million compared to \$6 million a year earlier.

Home Equity Servicing and Credit Quality

Our home equity lending business continues to service the majority of the loans it has securitized and sold. We earn a servicing fee of approximately 50 to 100 basis points of the outstanding principal balance of the loans securitized. The total servicing portfolio was \$2.4 billion at December 31, 2007 compared to \$2.9 billion at December 31, 2006. For whole loans sold with servicing retained totaling \$0.5 billion and \$0.7 billion at December 31, 2007 and 2006, respectively, we capitalize servicing fees including rights to future early repayment fees. During the first quarter of 2007, we adopted the fair value method under FAS 156. Adoption of this new standard resulted in a \$2.9 million increase in our servicing asset to adjust its value to fair market value. We recorded a one time (tax-affected) cumulative adjustment to retained earnings of \$1.7 million to reflect the adoption of this new standard. The servicing asset at December 31, 2007 was \$20 million, down from \$28 million at December 31, 2006 reflecting amortization with no new mortgage servicing rights additions.

Our managed portfolio, representing that portion of the servicing portfolio on which we have retained credit risk, is separated into two categories at December 31, 2007: \$1.5 billion of loans originated and held on balance sheet either as loans held for investment or loans held for sale, and \$0.1 billion of loans and lines of credit securitized for which we retained a residual interest. In both cases, we retain credit and interest rate risk.

Included below in the category *Credit Risk Sold, Potential Incentive Servicing Fee Retained Portfolio* are \$0.5 billion and \$0.6 billion of loans at December 31, 2007 and 2006, respectively, for which we have the opportunity to earn an incentive servicing fee. Although the credit performance of these loans we have sold is one factor that can affect the value of the incentive servicing fee, if these loans default, we do not bear the credit risk on these pools.

The credit quality of our portfolios declined substantially in 2007, reflecting declining economic conditions, increases in unemployment, and, apparently, significantly changed attitudes among consumers about the relative consequences of defaulting on their mortgage obligations. Net credit losses in 2007 increased 244% from 2006, rising to \$53 million. We expect further increases in 2008.

A disproportionate share of our realized and expected losses have arisen from a portfolio we originated prior to 2007 and held in *for sale* classification in early 2007. These loans were underwritten to third-party credit guidelines and as mortgage market conditions deteriorated in 2007, these third-party buyers left the market. Rather than selling into a depressed market, we reclassified these loans, approximately \$167 million, into *held-for-investment* status, having marked them to then current market. Throughout 2007, the credit quality of these loans continued to deteriorate, leading to heightened charge-offs and higher provisions. Realized losses on these loans totaled \$17 million during 2007. At December 31, 2007, our reserve for future losses on these transferred loans totaled \$22 million or 17% of their unpaid principal balance.

The following table sets forth certain information for our portfolios. The managed portfolio includes those loans we service with credit risk retained. Delinquency rates and losses on our managed portfolio result from a variety of factors, including loan seasoning, portfolio mix, and general economic conditions.

Included in the \$1.5 billion of unsold loans is approximately \$1.1 billion of loans which are funded through collateralized borrowings, as further explained in Footnote 11. While the Generally Accepted Accounting Principles

(GAAP) treatment of these loans is to present them as unsold as they fail sale treatment under SFAS 140 (i.e., we have not surrendered complete control of the assets), legally, these loans have been transferred to bankruptcy-remote trusts (securitization trusts). These trusts are the issuers of the asset-backed bonds which are shown on our balance sheet as collateralized notes. We retain an interest in excess cash flows and assets (if any) of the trust once the notes are paid off, which is called the overcollateralization. This distinction is important in ascertaining our retained risk in these loans. In short, while we bear some risk of loss on these securities loans, our loss is limited to the degree of overcollateralization we accepted in selling the loans to the securitization trusts. We

Table of Contents

are not obligated to, nor do we expect that we would, support the bonds issued by these trusts by providing cash or other security interest to the trusts in the future should the underlying home equity loan performance be insufficient to support debt service to bondholders. It should be noted that such a potential debt service short-fall to the bondholders would not be considered an event of default by Irwin as we are not the obligors on these securitization bonds. As of December 31, 2007, the overcollateralization embedded in the home equity securitization trusts, or the amount we have risk to future losses, totaled approximately \$150 million. In addition, unlike the loan sales historically made in the Discontinued Operations and to a limited degree, in this segment, the representations and warrants we make in selling loans to securitization trusts do not include loan performance based items. This has historically and we believe should continue to limit our loan repurchase risk in this segment.

	December 31,	
	2007	2006
	(Dollars in thousands)	
Managed Portfolio		
Total Loans	\$ 1,605,032	\$ 1,708,975
30 days past due	5.78%	3.16%
90 days past due	2.53	1.19
Net Chargeoff Rate	3.24	1.00
Unsold Loans		
Total Loans ⁽¹⁾	\$ 1,458,095	\$ 1,515,881
30 days past due	6.18%	3.54%
90 days past due	2.76	1.32
Net Chargeoff Rate	3.58	1.07
Loan Loss Reserve	\$ 91,700	\$ 33,614
Owned Residual		
Total Loans	\$ 146,937	\$ 193,094
30 days past due	1.83%	0.20%
90 days past due	0.29	0.18
Net Chargeoff Rate	0.17	0.42
Residual Undiscounted Losses	\$ 870	\$ 430
Credit Risk Sold, Potential Incentive Servicing Fee Retained Portfolio		
Total Loans	\$ 461,237	\$ 627,838
30 days past due	7.13%	5.40%
90 days past due	2.69	2.30

(1) Excludes deferred fees and costs.

Mortgage Banking (discontinued operations)

In 2006, we sold the mortgage banking line of business origination operation, including the majority of this segment's loans held for sale, as well as the majority of this segment's capitalized mortgage servicing rights to five separate purchasers. In January 2007, we transferred certain assets associated with this segment's servicing platform and placed the bulk of our remaining staff with a sixth buyer. Staff continue to work at IMC through the wind-down of our remaining assets, managing repurchased loans and collecting outstanding documents required for the completion of servicing transfers.

As discussed in Footnote 2 to the Financial Statements, we are reporting the results of our mortgage banking business as discontinued operations. In addition, certain of the remaining assets for this segment have been reclassified as held for sale in the consolidated balance sheet.

Table of Contents

Secondary market conditions negatively affected the wind-down. During the year, the discontinued segment lost \$31 million, compared to losses of \$36 million in 2006 and \$17 million in 2005. The majority of our current losses relate to credit costs for alleged breaches of representations and warrants made when loans were sold to the secondary market and, during the first portion of 2007, from early payment defaults. Our risk for repurchases for alleged breaches of representations and warrants extends through the life of the loans we originated prior to the sale of the segment in 2006 (whereas our obligation for repurchase due to early payment default typically lasts for approximately six months). Historically, the emergence period for the majority of these repurchase requests has been within three to four years after origination, but we experienced an increase in early-term repurchase requests due to early payment defaults and external fraud. It has now been approximately 18 months since we last originated a loan in this segment, so we expect claims arising due to borrower misrepresentation to subside in the near-term.

During 2007, requests for these repurchases increased materially in the first three quarters of the year before falling in the fourth quarter. Additionally, the principal cause of the repurchase requests changed meaningfully during the year, as a majority of the requests were based on the appearance of misrepresentation by borrowers or third-parties involved in the loan origination. To account for this increase in frequency and likely severity of loss from repurchased loans, during the third quarter we modified the method by which we estimate future loss risk. We used a statistical analysis to estimate future repurchase obligations. The analysis is based on a quantitative methodology similar to a vintage loss forecast, which projects losses based upon the age of loans. Loss curves have been developed based on historical data of repurchased loans, including the most recent activity where losses have been elevated. This analysis of historic actual repurchases is used to calculate expected lifetime and annual estimates of repurchases. As with vintage loss forecasts, this methodology takes into account differences in the quality of loans that were originated each year, as well as the likelihood of an investor demanding repurchase as loans age. Application of this revised analysis resulted in a repurchase liability of \$23 million at December 31, 2007.

The liability for repurchase risk does not include an estimate of amounts the Corporation may be able to recover from third parties on whom it relied in the origination of these loans it is now at risk of repurchasing. We believe this recovery effort could produce meaningful returns.

While we believe this liability reserve fully reflects our risk of loss in the current and expected environment, we are using these analyses to project losses during an environment with little precedent. These provisions and liabilities are based on current market conditions and our expectations of future losses that have not yet been incurred. Given that the period for which data is available for some vintages is very short, the extrapolation in the model may not be reliable and could result in significant changes to reserves derived from those vintages in future periods. We update the reserve analyses as more data is available.

Parent and Other

Results at the parent company and other businesses totaled a net loss of \$6.1 million for the year ended December 31, 2007, compared to losses of \$7.6 million during the same period in 2006 and \$0.8 million in 2005. These losses at the parent company primarily relate to operating and interest expenses in excess of management fees charged to the lines of business and interest income earned on intracompany loans. Included in parent company operating results are allocations to our subsidiaries of interest expense related to our interest-bearing capital obligations. During the year ended December 31, 2007, we allocated \$18 million of these expenses to our subsidiaries, compared to \$14 million and \$18 million during 2006 and 2005, respectively.

Each subsidiary pays taxes to us at the statutory rate. Subsidiaries also pay fees to us to cover direct and indirect services. In addition, certain services are provided from one subsidiary to another. Intercompany income and expenses are calculated on an arm's-length, external market basis and are eliminated in consolidation.

Risk Management

We are engaged in businesses that involve the assumption of risks including:

Credit risk

Liquidity risk

Table of Contents

Market risk (including interest rate and foreign exchange risk)

Operational risk

Compliance risk

The Board of Directors has primary responsibility for establishing the Corporation's risk appetite and overseeing its risk management system. Primary responsibility for management of risks within the risk appetite set by the Board of Directors rests with the managers of our business units, who are responsible for establishing and maintaining internal control systems and procedures that are appropriate for their operations. To provide an independent assessment of line management's risk mitigation procedures, we have established a centralized enterprise-wide risk management function. To maintain independence, this function is staffed with managers with substantial expertise and experience in various aspects of risk management who are not part of line management. They report to the Chief Risk Officer (CRO), who in turn reports to the Risk Committee of our Board of Directors. Our Internal Audit function independently audits both risk management activities in the lines of business and the work of the centralized enterprise-wide risk management function and reports directly to the Audit Committee of our Board of Directors.

Given the changes in the scope of the Corporation, our efforts to date to improve our risk management systems, and heightened industry and regulatory focus around credit, market, liquidity, operational and compliance risks, the Board, having reviewed and evaluated results of reports from Internal Audit, Risk Management, and regulatory exams, embarked in 2006 on a comprehensive review of our risk management systems. These assessments were conducted at the Board's direction by a third-party to ensure independence and access to best-in-class practices. As a result of these assessments, management has developed a program of risk management improvement steps that it has begun implementing on an enterprise-wide basis. As of December 31, 2007, we have substantially completed the actions required under this program and have turned attention to assuring we have systems in place to make these changes sustainable.

The objective of formal processes to manage risk is to ensure that risk is contained within the risk appetite established by our Board of Directors and expressed through policy guidelines and limits. In addition, we attempt to take risks only when we are adequately compensated for the level of risk assumed.

Our CEO, CFO, CAO, and Chief Risk Officer meet on a regularly-scheduled basis (or more frequently as appropriate) as an Enterprise-wide Risk Management Committee (ERMC), reporting to the Board of Directors' Risk Committee. Our Director of Internal Audit attends these meetings as an Observer. Our Chief Risk Officer, who reports directly to the Risk Committee, chairs the ERMC. To ensure coordination between Risk Committee and the Audit Committee, the Chair of each committee is a member of the other committee.

Each of our principal risks is managed directly at the line of business level, with oversight and, when appropriate, standardization provided by the ERMC and its subcommittees. The ERMC and its subcommittees oversee all aspects of our credit, market, operational and compliance risks. The ERMC provides senior-level review and enhancement of line of business risk management processes and oversight of our risk reporting and assessment and model parameter changes.

Credit Risk

The assumption of credit risk is a key source of our earnings. However, the credit risk in our loan portfolios has the most potential for a significant effect on our consolidated financial performance. Each of our segments has a Chief Credit Officer with expertise specific to the product line and manages credit risk through various combinations of the

use of lending policies, credit analysis and approval procedures, periodic loan reviews, servicing activities, and/or personal contact with borrowers. Commercial loans over a certain size, depending on the loan type and structure, are reviewed by a loan committee prior to approval. We perform independent loan review across the Corporation through a centralized function that reports directly to the head of Credit Risk Management who in turn reports to the Chief Risk Officer.

The allowance for loan and lease losses 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,

Table of Contents

Accounting by Creditors for Impairment of a Loan Income Recognition and Disclosures. The allowance is maintained at a level we believe is adequate to absorb probable losses inherent in the loan and lease portfolio. We perform an assessment of the adequacy of the allowance at the segment level no less frequently than on a quarterly basis and through review by a Committee chartered by the Board's Audit Committee.

Within the allowance, there are specific and general loss components. The specific loss component which applies to commercial loans, is based on a regular analysis of all loans over a fixed-dollar amount where the internal credit rating is at or below a predetermined classification. From this analysis we determine the loans that we believe to be impaired in accordance with SFAS 114. Management has defined impaired as nonaccrual loans. For loans determined to be impaired, we measure the level of impairment by comparing the loan's carrying 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 collateral value of the loan implies a value that is lower than carrying value. In addition to establishing allowance levels for specifically identified higher risk graded or delinquent loans, management determines an allowance for all other loans in the portfolio for which historical or projected experience indicates that certain losses will occur. These loans are segregated by major product type, and in some instances, by vintage, with an estimated loss ratio or migration pattern applied against each product type and vintage. For portfolios that are too new to have adequate historical experience on which to base a loss estimate, we use estimates derived from industry experience and management's judgment. The loss ratio or migration patterns are generally based upon historic loss experience or historic migration rate behaviors, respectively, for each loan type adjusted for certain environmental factors management believes to be relevant.

Net charge-offs for the year ended December 31, 2007 were \$64 million, or 1.2% of average loans, compared to \$20 million, or 0.4% of average loans during 2006. Net charge-offs in 2005 were \$11 million or 0.3% of average loans. The increase in charge-offs and allowance relates primarily to our home equity lending business. At December 31, 2007, the allowance for loan and lease losses was 2.5% of outstanding loans and leases and 1.4% at year-end 2006 and 1.3% in 2005.

Table of Contents

The following table shows an analysis of our consolidated allowance for loan and lease losses:

	2007	At or for the Year Ended December 31,			2003
		2006	2005	2004	
		(Dollars in thousands)			
Loans and leases outstanding at end of period, net of unearned income	\$ 5,696,230	\$ 5,238,193	\$ 4,477,943	\$ 3,440,689	\$ 3,147,094
Average loans and leases for the period, net of unearned income	\$ 5,486,727	\$ 4,854,368	\$ 3,875,394	\$ 3,312,785	\$ 3,151,325
Allowance for possible loan and lease losses:					
Balance beginning of period	\$ 74,468	\$ 59,223	\$ 43,441	\$ 63,005	\$ 50,320
Charge-offs:					
Commercial, financial and agricultural loans	9,160	3,503	2,976	3,262	4,263
Real estate mortgage loans	52,665	21,418	10,656	15,381	23,522
Consumer loans	1,846	328	723	351	765
Commercial Financing:					
Franchise financing	1,093	481	870	88	146
Domestic leasing	6,091	2,709	2,190	6,581	6,026
Canadian leasing	3,139	2,371	2,786	2,517	2,590
Total charge-offs	73,994	30,810	20,201	28,180	37,312
Recoveries:					
Commercial, financial and agricultural loans	597	576	767	318	77
Real estate mortgage loans	7,515	8,595	7,068	3,899	2,198
Consumer loans	197	154	85	169	248
Commercial Financing:					
Franchise financing		35	25		
Domestic leasing	1,313	923	583	626	448
Canadian leasing	477	925	432	323	449
Total recoveries	10,099	11,208	8,960	5,335	3,420
Net charge-offs	(63,895)	(19,602)	(11,241)	(22,845)	(33,892)
Reduction due to sale of loans	(1,225)		(403)	(627)	(234)
Reduction due to reclassification of loans		(246)		(10,808)	(690)
Foreign currency adjustment	519	(8)	119	243	582
Provision charged to expense	134,988	35,101	27,307	14,473	46,919
Balance end of period	\$ 144,855	\$ 74,468	\$ 59,223	\$ 43,441	\$ 63,005

Table of Contents

	At or for the Year Ended December 31,				
	2007	2006	2005	2004	2003
	(Dollars in thousands)				
Allowance for possible loan and lease losses by category:					
Commercial, financial and agricultural loans	\$ 33,667	\$ 25,593	\$ 19,927	\$ 18,126	\$ 20,571
Real estate mortgage loans	91,934	33,840	23,553	11,330	30,165
Consumer loans	1,462	1,510	4,879	4,242	809
Commercial Financing:					
Franchise financing	5,961	5,769	4,118	3,728	2,158
Domestic leasing	7,503	4,326	3,144	2,926	6,285
Canadian	4,328	3,430	3,602	3,089	3,017
Totals	\$ 144,855	\$ 74,468	\$ 59,223	\$ 43,441	\$ 63,005
Percent of loans and leases to total loans and leases by category:					
Commercial, financial and agricultural loans	37%	39%	42%	48%	48%
Real estate mortgage loans	40	40	39	33	36
Consumer loans	1	1	1	1	1
Commercial Financing:					
Franchise financing	11	9	7	7	5
Domestic leasing	4	5	5	4	4
Canadian	7	6	6	7	6
Ratios:					
Net charge-offs to average loans and leases ⁽¹⁾	1.2%	0.4%	0.3%	0.7%	1.1%
Allowance for possible loan losses to loans and leases outstanding	2.5%	1.4%	1.3%	1.3%	2.0%

Total nonperforming loans and leases at December 31, 2007, were \$76 million, compared to \$38 million at December 31, 2006, and \$37 million at December 31, 2005. Nonperforming loans and leases as a percent of total loans and leases at December 31, 2007 were 1.3%, compared to 0.7% at December 31, 2006, and 0.8% in 2005. The 2007 increase in nonperforming loans occurred across all three of our continuing lines of business with the largest increases attributable to commercial banking and home equity lending. Other real estate owned totaled \$15.6 million at December 31, 2007, up from \$15.2 million at the same date in 2006 and 2005. Total nonperforming assets at December 31, 2007 were \$93 million, or 1.5% of total assets. Nonperforming assets at December 31, 2006, totaled \$58 million, or 0.9% of total assets, compared to \$54 million, or 0.8%, in 2005.

Table of Contents

The following table shows information about our nonperforming assets at the dates shown:

	2007	2006	December 31, 2005	2004	2003
	(Dollars in thousands)				
Accruing loans past due 90 days or more:					
Commercial, financial and agricultural loans	\$ 177	\$	\$	\$	\$ 4,172
Real estate mortgages	151				
Consumer loans	41	73	455	645	226
Commercial financing:					
Franchise financing					151
Domestic leasing	311	83	73		8
Foreign leasing	177	236	71	12	70
	857	392	599	657	4,627
Nonaccrual loans and leases:					
Commercial, financial and agricultural loans	25,797	13,296	17,693	20,394	20,447
Real estate mortgages	40,681	18,125	14,237	8,510	14,663
Consumer loans	587	696	1,335	208	769
Commercial financing:					
Franchise financing	3,630	791	720	1,193	552
Domestic leasing	2,595	2,495	1,383	1,029	1,364
Foreign leasing	2,163	1,768	1,452	1,702	1,943
	75,453	37,171	36,820	33,036	39,738
Total nonperforming loans and leases	76,310	37,563	37,419	33,693	44,365
Nonperforming Loans held for Sale not guaranteed	79	5,564	965	2,066	1,695
Other real estate owned & other repossessed assets	16,885	15,170	15,226	9,427	6,431
Total nonperforming assets	\$ 93,274	\$ 58,297	\$ 53,610	\$ 45,186	\$ 52,491
Nonperforming loans and leases to total loans and leases	1.3%	0.7%	0.8%	1.0%	1.4%
Nonperforming assets to total assets	1.5%	0.9%	0.8%	0.9%	1.1%

For the periods presented, the year-end balances of any restructured loans are reflected in the table above either in the amounts shown for accruing loans past due 90 days or more or in the amounts shown for nonaccrual loans and leases.

The \$93 million of nonperforming assets at December 31, 2007, were concentrated at our lines of business as follows:

	December 31, 2007	December 31, 2006
	(In millions)	
Commercial banking	\$ 34	\$ 19
Commercial finance	10	5
Home equity lending	46	23
Mortgage banking	3	11

64

Table of Contents

Interest income of approximately \$5.5 million would have been recorded during 2007 on nonaccrual and renegotiated loans if such loans had been accruing interest throughout the year in accordance with their original terms. The amount of interest income actually recorded during the year of 2007 on nonaccrual and restructured loans was approximately \$2.4 million.

Generally, the accrual of income is discontinued when the full collection of principal or interest is in doubt, or when the payment of principal or interest has become contractually 90 days past due unless the obligation is both well secured and in the process of collection. Loans are charged-off upon evidence of expected loss or 180 days past due, whichever occurs first.

Liquidity Risk

Liquidity is the availability of funds to meet the daily requirements of our business. For financial institutions, demand for funds results principally from extensions of credit, withdrawal of deposits, and maturity of other funding liabilities. Liquidity is provided through deposits and short-term and long-term borrowings, by asset maturities or sales, and through equity capital.

The objectives of liquidity management are to ensure that funds will be available to meet current and future demands and that funds are available at a reasonable cost. Since loan assets are less marketable than securities and, therefore, need less volatile liability funding, the ratio of total loans to total deposits is a traditional measure of liquidity for banks and bank holding companies. At December 31, 2007, the ratio of loans (which excludes loans held for sale) to total deposits was 171%. We permanently fund a significant portion of our loans with secured financings, which effectively eliminates liquidity risk on these assets until we elected to exercise a clean up call. The ratio of loans to total deposits after reducing loans for those funded with secured financings was 126%.

As disclosed in the footnotes to the Consolidated Financial Statements, we have certain obligations to make future payments under contracts. At December 31, 2007, the aggregate contractual obligations are:

	Total	Payments Due by Period			
		One Year or Less	Over One to Three Years	Over Three to Five Years	After Five Years
Deposits with contractual maturity	\$ 1,548,982	\$ 1,094,464	\$ 380,741	\$ 66,628	\$ 7,149
Deposits without a stated maturity	1,776,506	1,776,506			
Other borrowings	802,424	456,912	179,241	100,667	65,604
Collateralized debt	1,213,139	305,094	414,472	470,081	23,492
Other long-term debt	233,878	5			233,873
Operating leases	40,964	10,228	16,817	9,385	4,534
Total	\$ 5,615,893	\$ 3,643,209	\$ 991,271	\$ 646,761	\$ 334,652

The table above describes our on-balance sheet contractual obligations. As described in the line of business sections, the home equity lending line of business historically funded a high percentage of their loan production via whole loan sales and/or asset securitization. Given the secondary market disruptions in 2007, we curtailed loan production

sharply.

Included in our long-term debt in the above table is subordinated debt of \$204 million that matures from 2032 to 2037; however, we may redeem the debentures at any time after five years from the date of issuance. These debentures are included in the maturity categories in the table above based on the maturity date.

Our deposits consist of two primary types: non-maturity transaction account deposits and certificates of deposit (CDs). Core deposits exclude jumbo CDs, brokered CDs, and public funds. Core deposits totaled \$2.3 billion at December 31, 2007 compared to \$2.4 billion at December 31, 2006.

Non-maturity transaction account deposits are generated by our commercial banking line of business and include deposits placed into checking, savings, money market and other types of deposit accounts by our customers. These types of deposits have no contractual maturity date and may be withdrawn at any time. While these balances

Table of Contents

fluctuate daily, a large percentage typically remains for much longer. At December 31, 2007, these deposit types totaled \$1.6 billion, a decrease of \$0.1 billion from December 31, 2006. We monitor overall deposit balances daily with particular attention given to larger accounts that have the potential for larger daily fluctuations and which are at greater risk to be withdrawn should there be an industry-wide or bank-specific event that might cause uninsured depositors to be concerned about the safety of their deposits. On a monthly basis we model the expected impact on liquidity from moderate and severe liquidity stress scenarios as one of our tools to ensure that our liquidity is sufficient.

CDs differ from non-contractual maturity accounts in that they do have contractual maturity dates. We issue CDs both directly to customers and through brokers. CDs issued directly to customers totaled \$0.5 billion at December 31, 2007, unchanged from December 31, 2006. Brokered CDs are typically considered to have higher liquidity (renewal) risk than CDs issued directly to customers, since brokered CDs are often done in large blocks and typically do not involve a direct relationship with the depositor. In recognition of this, we manage the size and maturity structure of brokered CDs closely. For example, the maturities of brokered CDs are laddered to mitigate liquidity risk. CDs issued through brokers totaled \$0.6 billion at December 31, 2007, and had an average remaining life of 17 months as compared to \$0.5 billion outstanding with a 17 month average remaining life at December 31, 2006.

Escrow account deposits are related to the servicing of our first mortgage loans. At December 31, 2007 these escrow balances totaled \$1.5 million, compared to \$0.3 billion at December 31, 2006. We sold the majority of our mortgage servicing rights in 2006 and transferred the servicing and related escrows in early 2007. These escrow deposits have been replaced in our funding profile by other deposit and borrowings.

Our largest borrowing source is the Federal Home Loan Bank of Indianapolis (FHLBI). We utilize their collateralized borrowing programs to help fund qualifying first mortgage, home equity and commercial real estate loans. As of December 31, 2007, FHLBI borrowings outstanding totaled \$0.6 billion, a \$0.2 billion increase from December 31, 2006. We had sufficient collateral pledged to FHLBI at December 31, 2007 to borrow an additional \$0.3 billion, if needed.

In addition to borrowings from the FHLBI, we use other lines of credit as needed. We have two lines of credit subject to compliance with certain financial covenants set forth in these facilities including, but not limited to, profitability and the level of nonperforming loans. Due to our net loss in 2007, we requested and obtained a waiver for a parent company credit facility with respect to certain net income related covenants. As a result of this waiver, we are in compliance with all applicable covenants as of December 31, 2007. Due to infrequent use of this credit facility (twice in the past two years only to test its availability), we have subsequently chosen to close this facility.

At December 31, 2007, the amount of other borrowings outstanding on our major credit lines and the total amount of the borrowing lines were as follows:

Lines of credit with correspondent banks, including fed funds lines: \$18 million outstanding out of \$175 million available but not committed

Lines of credit with non-correspondent banks, including fed funds lines: \$210 million outstanding

Warehouse lines of credit and conduits to fund Canadian sourced small ticket leases: \$242 million outstanding on \$391 million of borrowing facilities

In order to further diversify our funding sources, we have recently developed an internet deposit platform. Element Financial (<https://www.element-direct.com>) offers CDs nationally in denominations of \$5 thousand and larger. This initiative was released late in the second quarter of 2007 and, as a result, we had raised \$79 million of deposits

through this channel as of December 31, 2007.

We have a number of funding sources which are important to our operations. For example, we are a member (and customer) of the Federal Home Loan Bank of Indianapolis, we have a significant Canadian dollar funding facility with a single bank domiciled in Canada, and we have a significant deposit relationship with one of our commercial banking branches. In those instances where we have significant single relationships, on either the loan or funding side of the balance sheet, we examine each relationship more intensively than others and have developed contingency plans for the loss of these significant customer relationships. The loss of any one of these significant

Table of Contents

relationships would require changes to our funding program, but not in a manner which we would consider adversely material.

Market Risk (including Interest Rate and Foreign Exchange Risk)

Because all of our assets are not perfectly match-funded with like-term liabilities, our earnings are affected by interest rate changes. Interest rate risk is measured by the sensitivity of both net interest income and fair market value of net interest sensitive assets to changes in interest rates.

Our corporate-level asset-liability management committee (ALMC) oversees the interest rate risk profile of all of our lines of business. It is supported by ALMCs at each of our lines of business and monitors the repricing structure of assets, liabilities and off-balance sheet items. It uses a financial simulation model to measure the potential change in market value of all interest-sensitive assets and liabilities and also the potential change in earnings resulting from changes in interest rates. We incorporate many factors into the financial models, including prepayment speeds, prepayment fee income, deposit rate forecasts for non-maturity transaction accounts, caps and floors that exist on some variable rate instruments, embedded optionality and a comprehensive mark-to-market valuation process. We reevaluate risk measures and assumptions regularly, enhance modeling tools as needed, and, on an approximately annual schedule, have the model validated by internal audit or an out-sourced provider under internal audit's direction.

Our lines of business assume interest rate risk in the form of repricing structure mismatches between their loans and leases and funding sources. We manage this risk by adjusting the duration of their interest sensitive liabilities and through the use of hedging via financial derivatives.

Our commercial banking and home equity lines of business assume interest rate risk by holding MSR's (\$23 million at December 31, 2007). Among other items, a key determinant to the value of MSR's is the prevailing level of interest rates. The primary exposure to interest rates is the risk that rates will decline, possibly increasing prepayment speeds on loans and decreasing the value of MSR's. MSR's have traditionally been recorded at the lower of cost or fair market value. We adopted SFAS 156, Accounting for Servicing of Financial Assets on our high loan-to-value first lien and home equity segment second lien mortgages during the first quarter of 2007. This adoption requires full mark-to-market on the designated servicing assets, eliminating the lower-of-cost or market treatment. Our decisions on the degree to which we manage servicing right interest risk with derivative instruments to insulate against short-term price volatility depend on a variety of factors.

The following tables reflect our estimate of the present value of interest sensitive assets, liabilities, and off-balance sheet items at December 31, 2007. In addition to showing the estimated fair market value at current rates, they also provide estimates of the fair market values of interest sensitive items based upon a hypothetical instantaneous and permanent move both up and down 100 and 200 basis points in the entire yield curve.

The first table is an economic analysis showing the present value impact of changes in interest rates, assuming a comprehensive mark-to-market environment. The second table is an accounting analysis showing the same net present value impact, adjusted for expected GAAP treatment. Neither analysis takes into account the book values of the noninterest sensitive assets and liabilities (such as cash, accounts receivable, and fixed assets), the values of which are not directly determined by interest rates.

The analyses are based on discounted cash flows over the remaining estimated lives of the financial instruments. The interest rate sensitivities apply only to transactions booked as of December 31, 2007, although certain accounts are normalized whereby the three- or six-month average balance is included rather than the period-end balance in order to avoid having the analysis skewed by a significant increase or decrease to an account balance at period end.

The tables that follow should be used with caution.

The net asset value sensitivities do not necessarily represent the changes in the lines of business net asset value that would actually occur under the given interest rate scenarios, as sensitivities do not reflect changes in value of the companies as a going concern, nor consider potential rebalancing or other management actions that might be taken in the future under asset/liability management as interest rates change.

Table of Contents

The tables below show modeled changes in interest rates for individual asset and liability classes. Asset and liability classes in our portfolio have interest rate sensitivity tied to different underlying indices or instruments. While the rate sensitivity of individual classes presented below is our best estimate of changes in value due to interest rate changes, the total potential change figures are subject to basis risk if all yield curves do not move in parallel as the model assumes.

Few of the asset classes shown react to interest rate changes in a linear fashion. That is, the point estimates we have made at Current and +/-2% and +/-1% are appropriate estimates at those amounts of rate change, but it may not be accurate to interpolate linearly between those points. This is most evident in products that contain optionality in payment timing or pricing such as mortgage servicing or nonmaturity transaction deposits.

Finally, the tables show theoretical outcomes for dramatic changes in interest rates which do not consider potential rebalancing or repositioning of hedges and balance sheet mix.

Economic Value Change Method

	Present Value at December 31, 2007				
	Change in Interest Rates of:				
	-2%	-1%	Current	+1%	+2%
	(In thousands)				
Interest Sensitive Assets					
Loans and other assets	\$ 6,174,082	\$ 6,078,649	\$ 5,984,930	\$ 5,893,598	\$ 5,804,628
Loans held for sale	6,652	6,467	6,248	5,968	5,648
Mortgage servicing rights	17,894	21,052	24,766	27,441	29,196
Residual interests	11,831	11,947	12,047	12,184	12,269
Interest sensitive financial derivatives	(17,927)	(11,324)	(5,061)	955	7,009
Total interest sensitive assets	6,192,532	6,106,791	6,022,930	5,940,146	5,858,750
Interest Sensitive Liabilities					
Deposits	(3,287,120)	(3,256,158)	(3,227,564)	(3,194,925)	(3,160,041)
Short-term borrowings ⁽¹⁾	(1,075,226)	(1,062,628)	(1,050,608)	(1,039,129)	(1,028,158)
Long-term debt	(1,249,658)	(1,237,609)	(1,224,238)	(1,205,172)	(1,183,541)
Total interest sensitive liabilities	(5,612,004)	(5,556,395)	(5,502,410)	(5,439,226)	(5,371,740)
Net market value as of December 31, 2007	\$ 580,528	\$ 550,396	\$ 520,520	\$ 500,920	\$ 487,010
Change from current	\$ 60,008	\$ 29,876	\$	\$ (19,600)	\$ (33,510)
Net market value as of December 31, 2006	\$ 306,903	\$ 293,703	\$ 277,491	\$ 260,236	\$ 240,367
Potential change	\$ 29,412	\$ 16,212	\$	\$ (17,255)	\$ (37,124)

- (1) Includes certain debt which is categorized as collateralized debt in other sections of this document.

Table of Contents**GAAP-Based Value Change Method**

	Present Value at December 31, 2007				
	Change in Interest Rates of:				
	-2%	-1%	Current	+1%	+2%
	(In thousands)				
Interest Sensitive Assets					
Loans and other assets ⁽¹⁾	\$	\$	\$	\$	\$
Loans held for sale	6,134	6,134	6,134	5,855	5,534
Mortgage servicing rights	16,316	19,496	23,234	25,926	27,693
Residual interests	11,831	11,947	12,047	12,184	12,269
Interest sensitive financial derivatives	(17,927)	(11,324)	(5,061)	955	7,009
Total interest sensitive assets	16,354	26,253	36,354	44,920	52,505
Interest Sensitive Liabilities					
Deposits ⁽¹⁾					
Other borrowings ⁽¹⁾					
Long-term debt ⁽¹⁾					
Total interest sensitive liabilities ⁽¹⁾					
Net market value as of December 31, 2007	\$ 16,354	\$ 26,253	\$ 36,354	\$ 45,920	\$ 52,505
Potential change	\$ (20,000)	\$ (10,101)	\$	\$ 8,566	\$ 16,151
Net market value as of December 31, 2006	\$ 264,698	\$ 272,986	\$ 279,737	\$ 279,659	\$ 279,200
Potential change	\$ (15,039)	\$ (6,751)	\$	\$ (78)	\$ (537)

⁽¹⁾ Value does not change in GAAP presentation.

Off-Balance Sheet Instruments

In the normal course of our business as a provider of financial services, we are party to certain financial instruments with off-balance sheet risk to meet the financial needs of our customers. These financial instruments include loan commitments and standby letters of credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized on the consolidated balance sheet. We follow the same credit policies in making commitments and contractual obligations as we do for our on-balance sheet instruments. See Footnote 16 of the Financial Statements for further discussion related to guarantees.

Our exposure to credit loss, in the form of nonperformance by the counterparty on commitments to extend credit and standby letters of credit, is represented by the contractual amount of those instruments. Collateral pledged for standby letters of credit and commitments varies but may include accounts receivable; inventory; property, plant, and

equipment; and residential real estate. Total outstanding commitments to extend credit at December 31, 2007 and December 31, 2006, respectively, were \$1.1 billion and \$1.0 billion. We had \$22 million and \$25 million in irrevocable standby letters of credit outstanding at December 31, 2007 and December 31, 2006, respectively.

Derivative Financial Instruments

Financial derivatives are used as part of the overall asset/liability risk management process. We use certain derivative instruments that qualify and certain derivative instruments that do not qualify for hedge accounting treatment under SFAS 133. The derivatives that do not qualify for hedge treatment are classified as other assets and other liabilities and are marked to market on the income statement. While we do not seek Generally Accepted Accounting Principles (GAAP) hedge accounting treatment for the assets and liabilities that these instruments are hedging, the economic purpose of these instruments is to manage the risk inherent in existing exposures to either interest rate risk or foreign currency risk. For detail of our derivative activities, see Footnote 15 of our Consolidated Financial Statements.

Table of Contents

Operational and Compliance Risk.

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Irwin Financial, like other financial services organizations, is exposed to a variety of operational risks. These risks include reputational and legal risks, as well as the potential for processing or modeling errors, internal or external fraud, failure of computer systems, unauthorized access to information, and external events that are beyond the control of the Corporation, such as natural disasters.

Compliance risk is the risk of loss resulting from failure to comply with laws and regulations. While Irwin Financial is exposed to a variety of compliance risks, the two most significant arise from our consumer lending activities and our status as a public company.

Our Board of Directors has ultimate accountability for the level of operational and compliance risk we assume. The Board guides management by approving our business strategy and significant policies. Our management and Board have also established (and continue to improve) a control environment that encourages a high degree of awareness of the need to identify and alert senior management and the Board of potential control issues on a timely basis.

The Board has directed that primary responsibility for the management of operational and compliance risk rests with the managers of our business units, who are responsible for establishing and maintaining internal control procedures that are appropriate for their operations. Our enterprise-wide risk management function provides an independent assessment of line management's operational risk mitigation procedures. This function, which includes enterprise-wide oversight of compliance, reports to the Chief Risk Officer (CRO), who in turn reports to the Risk Committee of our Board of Directors. We have developed risk and control summaries for our key business processes. Line of business and corporate-level managers use these summaries to assist in identifying operational and other risks for the purpose of monitoring and strengthening internal and disclosure controls. Our Chief Executive Officer, Chief Financial Officer and Board of Directors, as well as the management committees of our subsidiaries, use the risk summaries to assist in overseeing and assessing the adequacy of our internal and disclosure controls, including the adequacy of our controls over financial reporting as required by section 404 of the Sarbanes Oxley Act and Federal Deposit Insurance Corporation Improvement Act.

Regulatory Environment

The financial services business is highly regulated. Failure to comply with these regulations could result in substantial monetary or other damages that could be material to our financial position. Statutes and regulations may change in the future. We cannot predict what effect these changes, if made, will have on our operations. It should be noted that the supervision, regulation and examination of banks, thrifts and mortgage companies by regulatory agencies are intended primarily for the protection of depositors and other customers rather than shareholders of these institutions.

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. 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. As an Indiana state chartered bank, our subsidiary, Irwin Union Bank and Trust, including its subsidiaries, is subject to examination by the Indiana Department of Financial Institutions and is also subject to examination, due to its membership in the Federal Reserve System, by the Federal Reserve. As a federal savings bank, our subsidiary Irwin Union Bank, F.S.B. is subject to examination by the Office of Thrift Supervision. The regulation, supervision and examinations of our enterprise occur at the local, state and federal levels and involve, but are not limited to, minimum capital requirements, consumer protection, community reinvestment, and deposit insurance.

Our subsidiary, Irwin Union Bank and Trust, entered into a memorandum of understanding, which is considered an informal agreement, with the Federal Reserve Bank of Chicago as of March 1, 2007 to enhance the consumer compliance function and compliance oversight programs of Irwin Union Bank and Trust and its subsidiaries. Irwin Union Bank and Trust agreed to and did provide quarterly written progress reports to the Federal Reserve Bank of Chicago with respect to these matters, through the required period ending September 30, 2007. We

Table of Contents

believe we have been responsive in developing and implementing plans to address the issues raised by the Federal Reserve Bank of Chicago. We are waiting for the Federal Reserve Bank of Chicago to perform a validation of the actions we took to address their concerns. However, if the Federal Reserve Bank of Chicago concludes the actions we took are not sufficient, we could experience additional regulatory action.

In consideration of the Corporation's capital position, on February 28, 2008, the Board of Directors elected to defer dividend payments on the Corporation's trust preferred securities and elected to discontinue payment of dividends on its non-cumulative perpetual preferred and common stock. Mindful of regulatory policy and the current economic environment, the Board took these steps to maintain the capital strength of the Corporation at a time of elevated uncertainty in the economy. The Board believes the elevated uncertainty in the current environment demands a greater bias to capital retention on a precautionary basis than distribution of cash from retained earnings for maintenance of historic dividends. The Board will reassess its dividend policy regularly. The ability to pay future dividends is subject to regulatory restrictions. See the discussions in *Part I, Supervision and Regulation* on *Dividends* under the *Bank Holding Company* section, and on *Dividend Limitations* under the *Bank and Thrift Regulation* section.

Item 7A. *Quantitative and Qualitative Disclosures about Market Risk*

The quantitative and qualitative disclosures about market risk are reported in the Market Risk section of Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations found on pages 67 through 69.

Item 8. *Financial Statements and Supplementary Data*

Management's Report on Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is a process designed under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America.

As of December 31, 2007, management conducted an assessment of the effectiveness of our internal control over financial reporting based on the framework established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, management has determined that internal control over financial reporting as of December 31, 2007 was effective.

Our effectiveness of internal control over financial reporting as of December 31, 2007 has been audited by Ernst & Young LLP, the independent registered public accounting firm that also audited our financial statements, as stated in their report which follows.

Table of Contents

Management also recognizes its responsibility for fostering a strong ethical climate so that our affairs are conducted according to the highest standards of personal and corporate conduct. This responsibility is articulated in our Guiding Philosophy, a condensed version of which has been published in our annual report since 1995 and more recently posted on our corporate web site. Employees at all levels of the Corporation are trained in our Guiding Philosophy. This responsibility is also reflected in our Code of Conduct. The Code of Conduct addresses, among other things, the necessity of ensuring open communication within Irwin Financial; potential conflicts of interest; compliance with all domestic and foreign laws, including those related to financial disclosures; and confidentiality of proprietary information. We maintain a systematic program to assess compliance with these policies.

-s- William I. Miller

William I. Miller
Chairman and
Chief Executive Officer

-s- Gregory F. Ehlinger

Gregory F. Ehlinger
Chief Financial Officer

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders of
Irwin Financial Corporation

We have audited Irwin Financial Corporation's internal control over financial reporting as of December 31, 2007, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Irwin Financial Corporation's management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Irwin Financial Corporation maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Irwin Financial Corporation as of December 31, 2007 and 2006, and the related consolidated statements of income, shareholders' equity, and cash flows for the years then ended and our report dated February 28, 2008 expressed an unqualified opinion thereon.

Chicago, Illinois
March 12, 2008

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders of
Irwin Financial Corporation

We have audited the accompanying consolidated balance sheets of Irwin Financial Corporation and subsidiaries as of December 31, 2007 and 2006, and the related consolidated statements of income, shareholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Irwin Financial Corporation and subsidiaries at December 31, 2007 and 2006, and the consolidated results of their operations and their cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 19 to the consolidated financial statements, during 2006 the Company changed its method of accounting for the recognition of share-based compensation expense.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Irwin Financial Corporation's internal control over financial reporting as of December 31, 2007, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 28, 2008 expressed an unqualified opinion thereon.

Chicago, Illinois
March 12, 2008

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Directors of
Irwin Financial Corporation:

In our opinion, the consolidated statements of income, shareholders' equity and cash flows for the year ended December 31, 2005 present fairly, in all material respects, the results of operations and cash flows of Irwin Financial Corporation and its subsidiaries for the year ended December 31, 2005, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

New York, New York
March 3, 2006, except for the effects of
discontinued operations discussed
in Note 2 to the consolidated
financial statements, as to which
the date is February 27, 2007

Table of Contents**IRWIN FINANCIAL CORPORATION AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS**

	December 31, 2007	December 31, 2006
	(Dollars in thousands)	
Assets:		
Cash and cash equivalents Notes 1 and 3	\$ 78,212	\$ 145,765
Interest-bearing deposits with financial institutions	31,841	53,106
Residual interests	12,047	10,320
Investment securities- held-to-maturity (Fair value: \$18,134 and \$17,893 at December 31, 2007 and 2006) Note 4	18,123	18,066
Investment securities- available-for-sale Note 4	59,684	47,776
Investment securities- other Note 4	62,588	62,588
Loans held for sale	6,134	237,510
Loans and leases, net of unearned income Note 5	5,696,230	5,238,193
Less: Allowance for loan and lease losses Note 6	(144,855)	(74,468)
	5,551,375	5,163,725
Servicing assets Note 7	23,234	31,949
Accounts receivable	38,710	208,585
Accrued interest receivable	26,291	26,470
Premises and equipment Note 8	38,178	36,211
Other assets	215,874	139,314
Assets held for sale Note 2	3,814	56,573
Total assets	\$ 6,166,105	\$ 6,237,958
Liabilities and Shareholders Equity:		
Deposits		
Noninterest-bearing	\$ 306,820	\$ 687,626
Interest-bearing	2,357,050	1,756,109
Certificates of deposit over \$100,000	661,618	1,107,781
	3,325,488	3,551,516
Other borrowings Note 10	802,424	602,443
Collateralized debt Note 11	1,213,139	1,173,012
Other long-term debt Note 12	233,873	233,889
Other liabilities	131,881	146,596
Total liabilities	5,706,805	5,707,456
Commitments and contingencies Notes 13, 14, and 16		
Shareholders equity		
Preferred stock, no par value authorized 4,000,000 shares;		
Noncumulative perpetual preferred stock 15,000 authorized and issued;	14,441	14,518

Edgar Filing: IRWIN FINANCIAL CORP - Form 10-K

Common stock, no par value authorized 40,000,000 shares; issued 29,896,464 shares and 29,879,773 as of December 31, 2007 and 2006; 670,169 and 143,543 shares in treasury as of December 31, 2007 and 2006	116,542	116,192
Additional paid-in capital	2,557	1,583
Accumulated other comprehensive income (loss), net of deferred income tax benefit of \$4,367 and \$4,813 as of December 31, 2007 and 2006	1,032	(4,364)
Retained earnings	337,524	405,835
	472,096	533,764
Less treasury stock, at cost	(12,796)	(3,262)
Total shareholders equity	459,300	530,502
Total liabilities and shareholders equity	\$ 6,166,105	\$ 6,237,958

The accompanying notes are an integral part of the consolidated financial statements.

Table of Contents**IRWIN FINANCIAL CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF INCOME**

	For the Year Ended December 31,		
	2007	2006	2005
	(Dollars in thousands, except per share)		
Interest income:			
Loans and leases	\$ 494,165	\$ 435,952	\$ 312,034
Loans held for sale	6,830	34,372	43,540
Residual interests	1,100	1,536	6,948
Investment securities	10,315	8,741	7,629
Federal funds sold	619	1,527	387
Total interest income	513,029	482,128	370,538
Interest expense:			
Deposits	137,360	132,221	83,861
Other borrowings	29,064	19,482	9,521
Collateralized debt	68,601	53,720	25,587
Other long-term debt	15,611	19,266	20,102
Total interest expense	250,636	224,689	139,071
Net interest income	262,393	257,439	231,467
Provision for loan and lease losses Note 6	134,988	35,101	27,307
Net interest income after provision for loan and lease losses	127,405	222,338	204,160
Other income:			
Loan servicing fees	19,275	32,844	39,678
Amortization of servicing assets Note 7	(1,199)	(21,027)	(31,014)
(Impairment) recovery of servicing assets Note 7	(10,946)	646	891
Net loan administration income	7,130	12,463	9,555
Gain from sales of loans	3,363	1,766	22,860
Trading gains	1,329	1,282	3,105
Derivative (losses) gains, net	(9,720)	3,820	(2,100)
Other	25,282	25,290	23,301
	27,384	44,621	56,721
Other expense:			
Salaries	97,028	107,864	110,463
Pension and other employee benefits	27,519	27,602	25,812
Office expense	9,316	9,130	8,587
Premises and equipment	23,539	22,748	21,286
Marketing and development	5,532	3,041	4,373
Professional fees	8,915	10,738	10,414

Edgar Filing: IRWIN FINANCIAL CORP - Form 10-K

Other	27,918	29,565	23,104
	199,767	210,688	204,039
(Loss) income before income taxes from continuing operations	(44,978)	56,271	56,842
Provision for income taxes	(20,848)	18,870	20,595
Net (loss) income from continuing operations	(24,130)	37,401	36,247
Loss from discontinued operations, net of \$20,581 and \$23,832 and \$11,613 income tax benefit, respectively Note 2	(30,543)	(35,674)	(17,260)
Net (loss) income	\$ (54,673)	\$ 1,727	\$ 18,987
Earnings per share from continuing operations: Note 20			
Basic	\$ (0.87)	\$ 1.27	\$ 1.27
Diluted	\$ (0.90)	\$ 1.25	\$ 1.26
Earnings per share: Note 20			
Basic	\$ (1.91)	\$ 0.06	\$ 0.67
Diluted	\$ (1.94)	\$ 0.05	\$ 0.66
Dividends per share	\$ 0.48	\$ 0.44	\$ 0.40

The accompanying notes are an integral part of the consolidated financial statements.

Table of Contents**IRWIN FINANCIAL CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY**

	Total	Retained Earnings	Foreign Currency	Accumulated Other Comprehensive Income			Deferred Compensation	Additional Paid in Capital	Common Stock	Preferred Stock
				Unrealized Gain/loss Securities	Unrealized Gain/loss Derivatives	Defined Benefit Plans				
January 1,	\$ 501,185	\$ 412,027	\$ 2,648	\$ 60	\$	\$ (254)	\$ (660)	\$ 383	\$ 112,000	\$
	18,987	18,987								
on securities	(433)			(433)						
benefit on net of	754				754					
y	693		693							
y										
P										
13 tax	(20)					(20)				
ensive	994									
ensive	19,981									
ensation	(99)						(99)			
stock	(11,426)	(11,426)								
s	617							617		
	(1,201)									
7 shares	3,277	(804)						(1,000)		
005	\$ 512,334	\$ 418,784	\$ 3,341	\$ (373)	\$ 754	\$ (274)	\$ (759)	\$	\$ 112,000	\$
	1,727	1,727								
on securities	29			29						
ability	(784)				(784)					

on ap y	(457)		(457)							
S: on and net of	91				91					
ensive	(1,121)									
ensive	606									
S 158, x 1	(6,691)				(6,691)					
S 123R	(13,110)	(13,110)					759	50		
stock	535							535		
s pense	1,742							1,742		
shares ares of	20,248	(1,058)							1,805	
shares ck	14,518									14,518
1 shares ck	2,387								2,387	
	(4,363)									
7 shares	2,296	(508)						(744)		
006	\$ 530,502	\$ 405,835	\$ 2,884	\$ (344)	\$ (30)	\$ (6,874)	\$	\$ 1,583	\$ 116,192	\$ 14,518
	(54,673)	(54,673)								
on rities benefit	(1,101)			(1,101)						
on ap net of fit	(1,546)				(1,546)					
y	6,274		6,274							
S:	1,769				1,769					

on and net of lity										
ensive	5,396									
ensive	(49,277)									
S 156,	1,743	1,743								
	(14,046)	(14,046)								
	(1,335)	(1,335)								
stock	91						91			
s ation	2,509						2,509			
costs	(77)									(77)
nmon										
	(12,804)									
6 shares	1,994						(1,626)	350		
007	\$ 459,300	\$ 337,524	\$ 9,158	\$ (1,445)	\$ (1,576)	\$ (5,105)	\$ 2,557	\$ 116,542	\$ 14,441	

The accompanying notes are an integral part of the consolidated financial statements.

Table of Contents**IRWIN FINANCIAL CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS**

	For the Years Ended December 31,		
	2007	2006	2005
	(Dollars in thousands)		
(Loss) income from continuing operations	\$ (24,130)	\$ 37,401	\$ 36,247
(Loss) from discontinued operations	(30,543)	(35,674)	(17,260)
Net (loss) income	(54,673)	1,727	18,987
Adjustments to reconcile net income to cash provided (used) by operating activities:			
Depreciation, amortization, and accretion, net	10,413	10,141	11,602
Amortization and impairment of servicing assets	12,395	61,370	80,697
Provision for loan and lease losses	134,988	35,288	26,852
Deferred income tax	(34,582)	(109,018)	(23,789)
Gain on sale of mortgage servicing assets		17,961	(14,412)
(Loss) gain from sales of loans held for sale	9,056	(39,754)	(98,127)
Originations and purchases of loans held for sale	(559,298)	(7,237,809)	(12,883,903)
Proceeds from sales and repayments of loans held for sale	791,712	8,262,743	12,502,574
Proceeds from sale of mortgage servicing assets	139	267,094	79,724
Net (increase) decrease in residuals	(627)	13,332	33,986
Net decrease (increase) in accounts receivable	169,875	(96,952)	10,246
Other, net	(49,706)	(100,215)	4,315
Net cash provided (used) by operating activities	429,692	1,085,908	(251,248)
Investing activities:			
Proceeds from maturities/calls of investment securities:			
Held-to-maturity	2,036	2,313	461
Available-for-sale	3,658	13,112	5,801
Purchase of investment securities:			
Held-to-maturity	(2,167)	(4,114)	
Available-for-sale	(17,455)	(23,197)	(3,599)
Net decrease (increase) in interest-bearing deposits	21,265	(1,976)	(3,985)
Net increase in loans, excluding sales	(485,986)	(820,664)	(1,115,391)
Proceeds from the sale of loans			57,625
Other, net	(9,100)	(11,376)	(8,331)
Net cash used by investing activities	(487,749)	(845,902)	(1,067,419)
Financing activities:			
Net (decrease) increase in deposits	(226,028)	(347,477)	503,730
Net (decrease) increase in other borrowings	199,981	(395,001)	760,167
Repayments of long-term debt	(16)	(14)	(12)
Proceeds from issuance of collateralized debt	364,579	931,406	472,515

Edgar Filing: IRWIN FINANCIAL CORP - Form 10-K

Repayments of collateralized debt	(324,505)	(427,373)	(351,049)
Proceeds from the issuance of trust preferred securities		61,500	51,750
Redemption of trust preferred securities		(77,509)	(51,750)
Proceeds from the sale of noncumulative perpetual preferred stock		14,518	
Purchase of treasury stock for employee benefit plans	(12,804)	(4,363)	(1,201)
Proceeds from sale of stock for employee benefit plans	2,085	7,740	3,277
Dividends paid	(15,381)	(13,110)	(11,426)
Net cash (used) provided by financing activities	(12,089)	(249,683)	1,376,001
Effect of exchange rate changes on cash	2,593	(44)	1,051
Net (decrease) increase in cash and cash equivalents	(67,553)	(9,721)	58,385
Cash and cash equivalents at beginning of period	145,765	155,486	97,101
Cash and cash equivalents at end of period	\$ 78,212	\$ 145,765	\$ 155,486
Supplemental disclosures of cash flow information:			
Cash flow during the period:			
Interest paid	\$ 251,019	\$ 239,934	\$ 146,005
Income taxes paid	\$ 13,098	\$ 93,687	\$ 19,171
Noncash transactions:			
Adoption of FAS 156	\$ 2,905	\$	\$
Transfer of loans from held for sale to held for investment	\$ 166,773	\$	\$
Other real estate owned	\$ 13,544	\$ 11,675	\$ 16,236
Conversion of trust preferred stock to common stock	\$	\$ 20,248	\$

The accompanying notes are an integral part of the consolidated financial statements.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 Summary of Significant Accounting Policies

Consolidation: Irwin Financial Corporation and its subsidiaries (the Corporation) provide financial services throughout the United States (U.S.) and Canada. We are engaged in commercial banking, commercial finance and home equity lending. We have exited the mortgage banking segment, maintaining a limited staff to manage our residual liabilities and responsibilities from past activities. Our direct and indirect subsidiaries include, Irwin Union Bank and Trust Company, Irwin Union Bank, F.S.B., Irwin Commercial Finance Corporation, Irwin Home Equity Corporation and Irwin Mortgage Corporation. Intercompany balances and transactions have been eliminated in consolidation. In the opinion of management, the financial statements reflect all material adjustments necessary for a fair presentation. The Corporation does not meet the criteria as primary beneficiary for our wholly-owned trusts holding our company-obligated mandatorily redeemable preferred securities established by Financial Accounting Standards Board (FASB) Interpretation No. 46 (FIN 46), Consolidation of Variable Interest Entities. As a result, these trusts are not consolidated.

For the mortgage banking line of business we have exited, the financial statements and footnotes within this report conform to the presentation required in Statement of Financial Accounting Standard (SFAS) 144, Accounting for the Impairment or Disposal of Long-Lived Assets for discontinued operations. Certain of the balance sheet assets and liabilities related to this line of business are being reported as assets held for sale. See Note 2 for additional information.

Use of Estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Foreign Currency: Assets and liabilities denominated in Canadian dollars are translated into U.S. dollars at rates prevailing on the balance sheet date; income and expenses are translated at average rates of exchange for the year. Unrealized foreign currency translation gains and losses are recorded in accumulated other comprehensive income in shareholders' equity.

Cash and Cash Equivalents: For purposes of the consolidated balance sheets, we consider cash and due from banks to be cash equivalents.

Investment Securities: Those investment securities that we have the positive intent and ability to hold until maturity are classified as held-to-maturity and are stated at cost adjusted for amortization of premiums and accretion of discounts (adjusted cost). All other investment securities are classified as available-for-sale and are stated at fair value. Unrealized gains and losses on available-for-sale investment securities, net of the future tax impact, are reported as a separate component of shareholders' equity until realized. Investment securities gains and losses are based on the amortized cost of the specific investment security determined on a specific identification basis.

Residual Interests: Residual interests are stated at fair value. Unrealized gains and losses are included in earnings. To obtain fair value of residual interests, quoted market prices would be used if available. However, quotes are generally not available for residual interests, so we estimate fair value based on the present value of expected cash flows using estimates of the key assumptions—prepayment speeds, credit losses, forward yield curves, and discount rates commensurate with the risks involved—that management believes market participants would use to value similar assets. Adjustments to carrying values are recorded as trading gains or losses.

Loans Held For Sale: Loans held for sale are carried at the lower of cost or market, determined on an aggregate basis for both performing and nonperforming loans. Cost basis includes deferred origination fees and costs. Fair value is determined based on the contract price at which the mortgage loans will be sold. At the time of origination, loans which management believes will be sold prior to maturity are classified as loans held for sale.

Table of Contents

Loans: Loans are carried at amortized cost. Loan origination fees and costs are deferred and the net amounts are amortized as an adjustment to yield using the interest method. When loans are sold, deferred fees and costs are included with outstanding principal balances to determine gains or losses. Interest income on loans is computed daily based on the principal amount of loans outstanding. The accrual of interest income is generally discontinued when a loan becomes 90 days past due as to principal or interest. Management may elect to continue the accrual of interest when the estimated net realizable value of collateral is sufficient to cover the principal balance and accrued interest and the loan is in the process of collection.

Direct Financing Leases: At lease inception, we record an asset representing the aggregate future minimum lease payments and deferred incremental direct costs less unearned income. Income is recognized over the life of the lease, which generally averages three to four years, in order to provide an approximate constant yield on the outstanding principal balance.

Allowance for Loan and Lease Losses: The allowance for loan and lease losses is an estimate based on management's 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. The allowance is maintained at a level we believe is adequate to absorb probable losses inherent in the loan and lease portfolio. We perform an assessment of the adequacy of the allowance on a quarterly basis.

Within the allowance, there are specific and expected loss components. The specific loss component is assessed for loans we believe to be impaired in accordance with 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 of that loan. 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 indicates that certain losses exist. 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.

It is our policy to promptly charge off any loan, or portion thereof, which is deemed to be uncollectible. This includes, but is not limited to, any loan rated Loss by the regulatory authorities. Impaired commercial credits are considered on a case-by-case basis. The amount charged off includes any accrued interest. Consumer loans are charged off when deemed uncollectible, but generally no later than when a loan is past due 180 days.

Servicing Assets: When we securitize or sell loans, we may retain the right to service the underlying loans sold. For cases in which we retain servicing rights, a portion of the cost basis of loans sold is allocated to a servicing asset based on its fair value relative to the loans sold and the servicing asset combined. Prior to the January 1, 2007, all servicing rights were carried at lower of cost or fair market value.

For servicing assets associated with second mortgages and high loan-to-value first mortgages, the fair value measurement method of reporting these servicing rights was elected beginning January 1, 2007, in accordance with SFAS 156, Accounting for Servicing of Financial Assets. Under the fair value method, we measure servicing assets at fair value at each reporting date and report changes in fair value in earnings in the period in which the changes occur. All remaining servicing rights follow the amortization method for subsequent measurement whereby these servicing rights are amortized in proportion to and over the period of estimated net servicing income.

We use a combination of observed pricing on similar, market-traded servicing rights and internal valuation models that calculate the present value of future cash flows to determine the fair value of the servicing assets. These models are supplemented and calibrated to market prices using inputs from independent servicing brokers, industry surveys and valuation experts. In using this valuation method, we incorporate assumptions that we believe market participants would use in estimating future net servicing income, which include, among other items, estimates of the cost of servicing per loan, the discount rate, float value, an inflation rate, ancillary income per loan, prepayment speeds, and default rates.

Table of Contents

Incentive Servicing Fees: For whole loan sales of certain home equity loans, in addition to our normal servicing fee, we have the right to an incentive servicing fee (ISF) that will provide cash payments to us if a pre-established return for the certificate holders and certain structure-specific loan credit and servicing performance metrics are met. Generally the structure-specific metrics involve both a delinquency and a loss test. The delinquency test is satisfied if, as of the last business day of the preceding month, delinquencies on the current pool of mortgage loans are less than or equal to a given percentage. The loss test is satisfied if, on the last business day of the preceding month, the percentage of cumulative losses on the original pool of mortgage loans is less than or equal to the applicable percentage as outlined in the specific deal documents. We receive ISF payments monthly, once the pre-established return has been paid to the certificate holder, if the delinquency and loss percentages are within guidelines. If we are terminated or replaced for cause as servicer under the securitization, the cash flow stream under the ISF contract terminates.

We account for ISFs similar to management contracts under Emerging Issues Task Force Topic No. D-96, Accounting for Management Fees Based on a Formula. Accordingly, we recognize revenue on a cash basis as the pre-established performance metrics are met and cash is due.

Derivative Instruments: All derivative instruments have been recorded at fair value and are classified as other assets or other liabilities in the consolidated balance sheets in accordance with SFAS 133, Accounting for Derivative Instruments and Hedging Activities.

Derivative instruments that are used in our risk management strategy may qualify for hedge accounting if the derivatives are designated as fair value, cash flow or foreign currency hedges and applicable hedge criteria are met. Changes in the fair value of a derivative that is highly effective (as defined by SFAS 133) and qualifies as a fair value hedge, along with changes in the fair value of the underlying hedged item, are recorded in current period earnings. Changes in the fair value of a derivative that is highly effective (as defined by SFAS 133) and qualifies as a cash flow hedge or foreign currency hedge, to the extent that the hedge is effective, are recorded in other comprehensive income until earnings are recognized from the underlying hedged item. Net gains or losses resulting from hedge ineffectiveness are recorded in current period earnings.

We use certain derivative instruments that do not qualify for hedge accounting treatment under SFAS 133. These derivatives are classified as other assets or other liabilities and marked to market in the consolidated income statements. While we do not seek hedge accounting treatment for these instruments, their economic purpose is to manage the risk of existing exposures to either interest rate risk or foreign currency risk.

Premises and Equipment: Premises and equipment are recorded at cost less accumulated depreciation. Depreciation is determined by the straight-line method over the estimated useful lives of the assets.

Other Assets: Included in other assets are real estate properties acquired as a result of foreclosure. These real estate properties are carried at the lower of the recorded investment in the related loan or fair value of the property less estimated costs to sell.

Income Taxes: A consolidated tax return is filed for all eligible entities. In accordance with SFAS 109, Accounting for Income Taxes, deferred income taxes are computed using the liability method, which establishes a deferred tax asset or liability based on temporary differences between carrying amounts and tax bases of assets and liabilities, computed using enacted tax rates.

Recent Accounting Developments: In March 2006, the FASB issued SFAS 156. This statement requires that all separately recognized servicing assets and servicing liabilities be initially measured at fair value, if practicable. The statement permits, but does not require, the subsequent measurement of classes of servicing assets and servicing

liabilities at fair value, to better align with the use of derivatives used to mitigate the inherent risks of these assets and liabilities. Offsetting changes in fair value are recognized through income. This statement was effective as of January 1, 2007. We elected the fair value treatment for servicing rights associated with second mortgage and high loan-to-value first mortgage loans at our home equity lending line of business. For all other servicing rights, we continue to use the amortization method. Implementation of the fair value treatment under SFAS 156 resulted in a one-time increase to retained earnings of \$1.7 million. This represents the after-tax effect of the \$2.9 million fair value adjustment to the mortgage servicing asset as of January 1, 2007.

Table of Contents

In September 2006, the FASB issued SFAS 157, Fair Value Measurements. This statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Based upon our evaluation of this new standard, it will not have a material impact on our financial statements.

In February 2007, the FASB issued SFAS 159, The Fair Value Option for Financial Assets and Financial Liabilities. This statement permits entities to choose to measure certain financial instruments at fair value. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007. We currently have no plans to implement this new elective standard in 2008.

Effective January 1, 2007, we adopted FASB Interpretation 48, Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109, (FIN 48), which prescribes a single, comprehensive model for how a company should recognize, measure, present and disclose in its financial statements uncertain tax positions that the company has taken or expects to take on its tax returns. Upon adoption of FIN 48, we did not recognize any material adjustment in our liability for unrecognized tax benefits (see Note 21).

Note 2 Discontinued Operations

In 2006 and early 2007, we sold the mortgage banking line of business origination operation including the majority of this segment's loans held for sale. Approximately \$0.3 billion of loans held for sale as well as certain other assets and liabilities were sold resulting in a loss of \$9 million including disposition costs. These losses are reflected in Loss from discontinued operations in the Consolidated Statement of Income. Loans and loans held for sale totaling \$2 million remain on our consolidated balance sheet and are classified as assets held for sale at December 31, 2007. These assets are carried at their fair value less costs to sell.

We also sold this segment's capitalized mortgage servicing rights. Mortgage servicing rights with an underlying unpaid principal balance of \$19 billion were sold to four unrelated parties resulting in a loss of \$21 million, which is reflected in Loss from discontinued operations in the Consolidated Statement of Income. The loss was partially offset by associated derivative gains of \$11 million. As a result of these sales, we are carrying \$31 million of receivables from these buyers at December 31, 2007.

In addition to the losses discussed above, we also incurred losses of \$10 million in connection with contract termination costs and severance benefits. These losses were recorded in accordance with SFAS 146, Accounting for Costs Associated with Exit or Disposal Activities. These losses are reflected in Loss from discontinued operations in the Consolidated Statement of Income. At December 31, 2007, there were \$2 million of accrued but unpaid expenses associated with our sale of the mortgage banking business.

In January 2007, we transferred certain assets associated with our servicing platform and placed the bulk of our remaining staff with New Century Financial. We have some staff continuing to work at Irwin Mortgage Corporation through the wind-down of our remaining assets, such as repurchased loans.

In accordance with the provisions of SFAS 144, the results of operations of the mortgage banking line of business for the current and prior periods have been reported as discontinued operations. In addition, certain of the remaining assets for this segment have been reclassified as held for sale on the consolidated balance sheet.

Results for this discontinued portion of our business are as follows:

	For the Year Ended December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Net revenues	\$ (17,190)	\$ 37,983	\$ 98,643
Other expense	(33,934)	(97,489)	(127,516)
Loss before income taxes	(51,124)	(59,506)	(28,873)
Income taxes	20,581	23,832	11,613
Net loss from discontinued operations	\$ (30,543)	\$ (35,674)	\$ (17,260)

Table of Contents

	December 31,	
	2007	2006
	(Dollars in thousands)	
Loans, net of allowance and Loans held for sale	\$ 1,281	\$ 48,555
Net servicing asset		385
Other assets	2,533	7,633
Assets held for sale	\$ 3,814	\$ 56,573

Note 3 Restrictions on Cash and Dividends

Irwin Union Bank and Trust Company and Irwin Union Bank, F.S.B. are required to maintain minimum average noninterest bearing reserve balances with the Federal Reserve Bank. At December 31, 2007, we exceeded this requirement.

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 addition to the limitations imposed by Indiana Law, 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. As a result of our losses in 2007, the bank cannot declare a dividend to us without regulatory approval until such time that current year earnings plus earnings from the last two years exceeds dividends during the same periods. We sought and were granted such approval for a \$15 million dividend in the second quarter of 2007. Our ability to pay dividends in the future on our Trust Preferred, non-cumulative perpetual preferred, and common stock is dependent on our ability to dividend from Irwin Union Bank and Trust, for which prior regulatory approval will be necessary from the Indiana Department of Financial Institutions and the Federal Reserve Bank of Chicago.

In consideration of the Corporation's capital position, on February 28, 2008, the Board of Directors elected to defer dividend payments on the Corporation's trust preferred securities and elected to discontinue payment of dividends on its non-cumulative perpetual preferred and common stock. These steps are being undertaken to maintain the capital strength of the Corporation at a time of elevated uncertainty in the economy.

Interest on the subordinated debt underlying the trust preferred securities will continue to accrue at its scheduled rate and cash dividends will be paid to holders prior to the resumption of dividends on the non-cumulative perpetual preferred and common stock.

The board took action on the perpetual preferred and common stock as it believes, in a total stakeholder balance, that the elevated uncertainty in the current environment demands a greater bias to capital retention on a precautionary basis than distribution of cash from retained earnings for maintenance of historic dividends.

The Board will reassess its dividend policy regularly, with an eye towards resuming the cash payment of the deferred dividends on trust preferred securities and recommencing dividends on the non-cumulative perpetual preferred and

common stock once the level of uncertainty in the current market declines and the profitability of the Corporation supports such dividends. The ability to pay future dividends will be subject to the regulatory restrictions discussed above.

Table of Contents**Note 4 Investment Securities**

The amortized cost, fair value, and carrying value of investment securities held at December 31, 2007 were as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Carrying Value
	(Dollars in thousands)				
Held-to-Maturity:					
U.S. Treasury and government obligations	\$ 13,970	\$ 68	\$ (42)	\$ 13,996	\$ 13,970
Obligations of states and political subdivisions	3,436			3,436	3,436
Mortgage-backed securities	717		(14)	702	717
Total held-to-maturity	18,123	68	(56)	18,134	18,123
Available-for-Sale:					
Mortgage-backed securities	46,898	20	(1,419)	45,499	45,499
Other	15,196		(1,011)	14,185	14,185
Total available-for-sale	62,094	20	(2,430)	59,684	59,684
Federal Home Loan Bank and Federal Reserve Bank stock	62,588			62,588	62,588
Total investment securities	\$ 142,805	\$ 88	\$ (2,486)	\$ 140,406	\$ 140,395

The amortized cost, fair value, and carrying value of investment securities held at December 31, 2006 were as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Carrying Value
	(Dollars in thousands)				
Held-to-Maturity:					
U.S. Treasury and government obligations	\$ 13,730	\$	\$ (156)	\$ 13,574	\$ 13,730
Obligations of states and political subdivisions	3,545			3,545	3,545
Mortgage-backed securities	791	2	(19)	774	791
Total held-to-maturity	18,066	2	(175)	17,893	18,066
Available-for-Sale:					
Mortgage-backed securities	44,907	44	(555)	44,396	44,396
Other	3,443		(63)	3,380	3,380

Edgar Filing: IRWIN FINANCIAL CORP - Form 10-K

Total available-for-sale	48,350	44	(618)	47,776	47,776
Federal Home Loan Bank and Federal Reserve Bank stock	62,588			62,588	62,588
Total investment securities	\$ 129,004	\$ 46	\$ (793)	\$ 128,257	\$ 128,430

Table of Contents

The following table presents the fair value and unrealized losses for certain available-for-sale securities by aging category:

	Securities with Unrealized Losses at December 31, 2007					
	Less than 12 Months		12 Months or More		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
	(Dollars in thousands)					
Mortgage backed securities	\$ 14,714	\$ (775)	\$ 25,959	\$ (644)	\$ 40,673	\$ (1,419)
Other securities	15,196	(1,011)			15,196	(1,011)
Total securities with unrealized losses	\$ 29,910	\$ (1,786)	\$ 25,959	\$ (644)	\$ 55,869	\$ (2,430)

Impairment is evaluated considering numerous factors, and their relative significance varies case to case. Factors considered include the length of time and extent to which the market value has been less than cost; the financial condition and near-term prospects of the issuer; and the intent and ability to retain the security in order to allow for an anticipated recovery in market value. If, based on the analysis, it is determined that the impairment is other-than-temporary, the security is written down to fair value, and a loss is recognized through earnings.

Included in the \$2.4 million of gross unrealized losses on the available-for-sale securities at December 31, 2007, was \$0.6 million of unrealized losses that have existed for a period greater than 12 months. These securities are U.S. government backed or have AA or better credit enhancements and the unrealized losses are not due to concerns about underlying credit quality. Substantially all of the securities with the unrealized losses aged greater than 12 months have a market value at December 31, 2007, that is within 7% of their amortized cost basis. We have the positive intent and ability to hold these securities until maturity. Accordingly, we have concluded that none of the securities in our investment portfolios are other-than-temporarily impaired at December 31, 2007.

The amortized cost and estimated value of investment securities at December 31, 2007, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
	(Dollars in thousands)	
Held-to-Maturity:		
Due within one year	\$ 4,229	\$ 4,117
Due after one year through five years	9,741	9,879
Due after ten years	3,436	3,436
	17,406	17,432
Mortgage-backed securities	717	702

	18,123	18,134
Available-for-Sale:		
Due in one year or less	15,196	14,185
Mortgage-backed securities	46,898	45,499
	62,094	59,684
Federal Home Loan Bank & Federal Reserve Bank stock	62,588	62,588
Total investment securities	\$ 142,805	\$ 140,406

Investment securities of \$20 million were pledged and cannot be repledged by holder, as collateral for borrowings and for other purposes on December 31, 2007. During 2007 and 2006 there were no sales or calls on investment securities.

Table of Contents**Note 5 Loans and Leases**

Loans and leases are summarized as follows:

	December 31,	
	2007	2006
	(Dollars in thousands)	
Commercial, financial and agricultural	\$ 2,099,451	\$ 2,025,890
Real estate-construction & land development	586,037	601,699
Real estate-mortgage	1,691,450	1,522,616
Consumer	32,232	31,581
Commercial financing		
Franchise financing	925,741	699,969
Domestic leasing	306,301	296,056
Foreign leasing	462,036	358,783
Unearned income		
Franchise financing	(306,681)	(211,480)
Domestic leasing	(42,723)	(42,782)
Foreign leasing	(57,614)	(44,139)
Total	\$ 5,696,230	\$ 5,238,193

At December 31, 2007, mortgage loans and leases held for investment with a carrying value of \$1.5 billion were pledged as collateral for bonds payable to investors (See Note 11).

Federal Home Loan Bank borrowings are collateralized by \$1.4 billion in loans and loans held for sale at December 31, 2007.

Commercial loans are extended primarily to local regional businesses in the market areas of our commercial banking line of business. To a lesser extent, we also provide consumer loans to the customers in those markets. Real estate loans, franchise loans and direct financing leases are extended throughout the United States and Canada.

We make loans to directors and officers, and to organizations and individuals with which our directors and officers are associated. All outstanding loans and commitments included in such transactions were made in the normal course of business and on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other persons and did not involve more than the normal risk of collectibility or present other unfavorable features. All such loans outstanding at December 31, 2007 were current in payment of principal and interest. The aggregate dollar amount of these loans outstanding at December 31, 2007 and 2006 represented approximately 1% of total equity.

We offer home equity loans with combined loan-to-value (CLTV) ratios of up to 125% of their collateral value. Home equity loans are priced using a proprietary model, taking into account, among other factors, the credit history of our customer and the relative loan-to-value (LTV) ratio of the loan at origination. For the year ended December 31, 2007, home equity loans with loan-to-value ratios greater than 100% (high LTVs, or HLTVs) made up 51% of our loan originations and 55% of our managed portfolio. HLTVs constituted 47% of our managed portfolio at December 31, 2006. The higher concentration in 2007 is due to the mix of retained production in 2007 and faster paydowns on

non-HLTV product during the year. In an effort to manage portfolio concentration risk and to comply with existing banking regulations, we have policies in place governing the size of our investment in loans secured by real estate where the LTV is greater than 90%.

We finance a variety of commercial, light industrial and office equipment types and try to limit the concentrations in our loan and lease portfolios. The majority of our leases are full payout (no residual), small-ticket assets secured by commercial equipment.

Table of Contents

The following lists the components of the net investment in leases:

	December 31,	
	2007	2006
	(Dollars in thousands)	
Minimum lease payments receivable	\$ 757,609	\$ 644,118
Initial direct costs	10,728	10,721
Less unearned income	(100,337)	(86,921)
Less allowance for lease losses	(11,206)	(7,756)
Net investment in leases	\$ 656,794	\$ 560,162

Note 6 Allowance for Loan and Lease Losses and Nonperforming Loans and Leases

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

	December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Balance at beginning of year	\$ 74,468	\$ 59,223	\$ 43,441
Provision for loan and lease losses	134,988	35,101	27,307
Charge-offs	(73,994)	(30,810)	(20,201)
Recoveries	10,099	11,208	8,960
Reduction due to reclassification and sales of loans	(1,225)	(246)	(403)
Foreign currency adjustment	519	(8)	119
Balance at end of period	\$ 144,855	\$ 74,468	\$ 59,223

Impaired loans and associated valuation reserves are summarized as follows:

	December 31,	
	2007	2006
	(Dollars in thousands)	
Impaired loans with valuation reserve	\$ 22,889	\$ 10,893
Impaired loans with no valuation reserve	4,420	3,476
Total impaired loans	\$ 27,309	\$ 14,369
Valuation reserve on impaired loans	\$ 6,519	\$ 3,086

Interest accrued but not collected at the date a loan is considered impaired is reversed against interest income. Interest income on impaired loans is recognized on a cash basis as long as the remaining book balance is deemed fully collectible. If the future collectibility of the recorded loan balance is doubtful, any collections of interest and principal are generally applied as a reduction to principal outstanding. The accrual of interest is reestablished only when interest and principal payments are brought current and future payments are reasonably assured. For the year ended December 31, 2007, the average balance of impaired loans was \$20 million, for which \$1.9 million of interest was recorded. For the years ended December 31, 2006 and 2005, respectively, \$0.8 million and \$1.0 million of interest income was recorded on average impaired loans balances of \$13 million and \$17 million, respectively.

Nonperforming loans and leases are summarized below:

	December 31,	
	2007	2006
	(Dollars in thousands)	
Accruing loans past due 90 days or more	\$ 857	\$ 392
Nonaccrual loans and leases	75,453	37,171
Total nonperforming loans and leases	\$ 76,310	\$ 37,563

Table of Contents**Note 7 Servicing Assets**

We adopted the fair value treatment for servicing assets associated with our second mortgage and high loan-to-value first mortgage portfolios as of January 1, 2007. The effect of remeasuring the selected servicing assets at fair value was reported as a cumulative-effect adjustment to retained earnings, increasing retained earnings \$1.7 million, net of tax. Changes in fair value subsequent to adoption were recorded through impairment/recovery of servicing assets. All other servicing assets, primarily related to first mortgage loans, continue to be accounted for using the amortization method with impairment recognized. These mortgage servicing assets are recorded at 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 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 adversely affect our results of operations. For servicing rights accounted for under the amortization method, we also review these mortgage servicing assets 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.

Changes in our fair value servicing assets are shown below:

	December 31,	
	2007	2006
	And the Year Then	
	Ended	
	(Dollars in thousands)	
Beginning balance	\$ 27,725	NA
Gain from initial adoption of SFAS 156	2,905	NA
Changes in fair value:		
Due to changes in valuation inputs or assumptions ⁽¹⁾	(1,589)	NA
Other changes in fair value ⁽²⁾	(9,317)	NA
Mortgage servicing assets	\$ 19,724	NA

(1) Principally reflects changes in discount rates and prepayment speed assumptions, primarily due to changes in interest rates.

(2) Represents changes due to realization of expected cash flows.

Table of Contents

Changes in our amortizing servicing assets are shown below:

	December 31, 2007 2006 And the Year Then Ended (Dollars in thousands)	
Beginning balance	\$ 31,949	\$ 295,754
Initial adoption of SFAS 156	(27,725)	
Additions	530	83,005
Sales	(5)	(285,055)
Amortization	(1,199)	(61,699)
(Impairment) recovery	(40)	329
Mortgage servicing assets	3,510	32,334
Less servicing asset from discontinued operations		385
Mortgage servicing asset from continuing operations	\$ 3,510	\$ 31,949

We have established a valuation allowance to record servicing assets at their fair market value. Changes in the allowance are summarized below:

	December 31, 2007 2006 And the Year Then Ended	
Balance at beginning of year	\$ 483	\$ 27,243
Transfer of assets from amortizing to fair value	(332)	
Impairment (recovery)	40	(329)
Reclass for sales of servicing and clean up calls		(26,431)
Valuation allowance from continuing operations	\$ 191	\$ 483

The servicing assets had a fair value of \$25 million and \$37 million at December 31, 2007 and 2006, respectively. At December 31, 2007, key economic assumptions and the sensitivity of the current carrying value of mortgage servicing rights to immediate 10% and 20% adverse changes in those assumptions are as follows (dollars in thousands):

Fair value of mortgage servicing assets	\$ 24,766
Constant prepayment speed	21.95%
Impact on fair value of 10% adverse change	\$ (1,036)

Impact on fair value of 20% adverse change	(1,973)
Discount rate	11.70%
Impact on fair value of 10% adverse change	\$ (544)
Impact on fair value of 20% adverse change	(988)

These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in value based on a 10% and 20% variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in value may not be linear. Also, in this table, the effect of a variation in a particular assumption on the value of the servicing asset is calculated without changing any other assumption; in reality, changes in one factor may result in changes in another (for example, increases in market interest rates may result in lower prepayments), which might magnify or counteract the sensitivities.

Table of Contents

The servicing portfolio underlying the portion of our servicing assets carried on our balance sheet was \$2.2 billion and \$2.8 billion at December 31, 2007 and 2006, respectively. Key economic assumptions used in determining the carrying value of mortgage servicing assets capitalized in 2007 and 2006 were as follows:

	2007	2006
Prepayment rates (range):	3 to 35%	3 to 39%
Discount rates (range):	9 to 15%	9 to 15%

Note 8 Premises and Equipment

Premises and equipment are summarized as follows:

	2007	December 31, 2006	Useful Lives
(Dollars in thousands)			
Land	\$ 3,302	\$ 3,584	n/a
Building and leasehold improvements	30,827	28,931	7-40 years
Furniture and equipment	54,611	52,786	3-10 years
	88,740	85,301	
Less accumulated depreciation	(50,562)	(49,090)	
Total	\$ 38,178	\$ 36,211	

Amounts charged to other expense for depreciation were \$7.1 million, \$6.4 million, and \$7.3 million in 2007, 2006, and 2005, respectively.

Note 9 Lease Obligations

At December 31, 2007, we leased certain branch locations and office equipment used in our operations under a number of noncancelable operating leases. Operating lease rental expense was \$11 million in 2007, \$18 million in 2006, and \$23 million in 2005.

The future minimum rental payments required under noncancellable operating leases with initial or remaining terms of one year or more are summarized as follows:

	(Dollars in thousands)	
Year Ended December 31,		
2008	\$	10,228
2009		9,001
2010		7,816
2011		6,675

2012		2,710
Thereafter		4,534
Total minimum rental payments	\$	40,964

Table of Contents**Note 10 Other borrowings**

Other borrowings are summarized as follows:

	December 31,	
	2007	2006
	(Dollars in thousands)	
Federal Home Loan Bank borrowings	\$ 574,424	\$ 371,693
Drafts payable related to mortgage loan closings		250
Federal funds	228,000	230,500
Total	\$ 802,424	\$ 602,443
Weighted average interest rate	5.20%	4.49%

Federal Home Loan Bank borrowings are collateralized by \$1.4 billion of loans and loans held for sale at December 31, 2007.

In addition to borrowings from the FHLB, we use other lines of credit as needed. We also have lines of credit available of \$0.4 billion to fund loan originations and operations. Interest on the lines of credit is payable monthly or quarterly with rates ranging from 3.3% to 6.3% at December 31, 2007. We have one line of credit subject to compliance with certain financial covenants set forth in this facility including, but not limited to, profitability and the level of nonperforming loans. Due to our net loss in 2007, we requested and obtained a waiver for this credit facility with respect to certain net income related covenants. As a result of this waiver, we are in compliance with all applicable covenants as of December 31, 2007. Due to infrequent use of this credit facility (twice in the past two years only to test its availability), we have subsequently chosen to close this facility.

Note 11 Collateralized Debt

We pledge loans in transactions structured as secured financings at our home equity and commercial finance lines of business. Sale treatment is precluded on these transactions because we fail the true-sale requirements of SFAS 140 as we maintain effective control over the loans and leases securitized. This type of structure results in cash being received, debt being recorded, and loans being retained on the balance sheet. The notes associated with these transactions are collateralized by \$1.5 billion in home equity loans, home equity lines of credit, and leases. The principal and interest on these debt securities are paid using the cash flows from the underlying loans and leases. Accordingly, the timing of the principal payments on these debt securities is dependent on the payments received on the underlying collateral. The interest rates on the bonds are both fixed and floating.

Table of Contents

Collateralized borrowings are summarized as follows:

	Contractual Maturity	Weighted Average Interest Rate at December 31, 2007 (Dollars in thousands)	December 31, 2007	December 31, 2006
Commercial finance line of business				
Domestic asset backed note			\$	\$ 5,797
Canadian asset backed notes:				
Note 1	revolving	5.7%	46,183	30,611
Note 2	9/2012	5.3	192,103	179,508
Note 3	10/2009	4.5	4,120	8,157
Home equity line of business				
2004-1 asset backed notes:				
Variable rate senior note	12/2024-12/2034	5.1	33,733	50,072
Variable rate subordinate note	12/2034	6.0	24,775	24,775
2005-1 asset backed notes:				
Variable rate senior note	6/2025-6/2035	5.0	23,484	40,972
Fixed rate senior note	6/2035	5.2	59,471	94,129
Variable rate subordinate note	6/2035	6.6	10,785	10,785
Fixed rate subordinate note	6,2035	5.6	52,127	52,127
Unamortized premium/discount			(62)	(90)
2006-1 asset backed notes:				
Variable rate senior note	9/2035	5.0	44,302	102,252
Fixed rate senior note	9/2035	5.5	96,561	96,561
Fixed rate lockout senior note	9/2035	5.6	24,264	24,264
Unamortized premium/discount			(12)	(19)
2006-2 asset backed notes:				
Variable rate senior note	2/2036	4.9	82,945	136,386
Fixed rate senior note	2/2036	6.3	80,033	80,033
Fixed rate lockout senior note	2/2036	6.2	21,348	21,348
Unamortized premium/discount			(13)	(21)
2006-3 asset backed notes:				
Variable rate senior note	1/2037-9/2037	4.9	83,281	130,326
Fixed rate senior note	9/2037	5.9	67,050	67,050
Fixed rate lockout senior note	9/2037	5.9	18,000	18,000
Unamortized premium/discount			(7)	(11)
2007-1 asset backed notes:				
Variable rate senior note	8/2037	4.9	135,339	
Fixed rate senior note	8/2037	6.0	91,346	
Fixed rate lockout senior note	8/2037	5.9	22,000	
Unamortized premium/discount			(17)	
Total			\$ 1,213,139	\$ 1,173,012

Table of Contents**Note 12 Other Long-Term Debt**

At December 31, 2007 we had \$234 million of other long-term debt, unchanged from 2006. Included in both years is \$30 million of subordinated debt with an interest rate of 7.58% and a maturity date of July 2014. We also have obligations represented by subordinated debentures at December 31, 2007 and 2006 of \$204 million. These securities were issued by wholly-owned trusts of Irwin Financial Corporation that were created for the purpose of issuing cumulative trust preferred securities. In accordance with FIN 46 we do not consolidate these trusts. These debentures are the sole assets of these trusts as of December 31, 2007. All debentures and securities are callable at par after five years from origination date.

These securities are all Tier 1 qualifying capital at December 31, 2007. Highlights about these debentures and the related trusts are listed below:

Name	Origination Date	Interest Rate at December 31, 2007	Maturity Date	Subordinated Debt December 31,		Other
				2007	2006	
IFC Capital Trust VI	Oct 2002	8.70	Sep 2032	\$ 35,567	\$ 35,567	fixed rate for term
IFC Statutory Trust VII	Nov 2003	7.73	Nov 2033	51,547	51,547	rate changes quarterly at three month LIBOR plus 290 basis points
IFC Capital Trust VIII	Aug 2005	5.96	Aug 2035	53,351	53,351	fixed rate for 5 years, variable rate of 3 month LIBOR plus 153 basis points thereafter
IFC Capital Trust IX	Mar 2006	6.69	Mar 2036	32,475	32,475	fixed rate for 5 years, variable rate of 3 month LIBOR plus 149 basis points thereafter
IFC Capital Trust X	Dec 2006	6.53	Dec 2036	15,464	15,464	fixed rate for 5 years, variable rate of 3 month LIBOR plus 175 basis points thereafter
IFC Capital Trust XI	Dec 2006	6.89	Mar 2037	15,464	15,464	variable rate of 3 month LIBOR plus 174 basis

points

\$ 203,868 \$ 203,868

Note 13 Commitments and Contingencies*Culpepper v. Inland Mortgage Corporation*

On February 29, 2008, the United States Court of Appeals for the 11th Circuit denied the plaintiffs' petition for rehearing and petition for rehearing en banc. The denial let stand the 11th Circuit's July 2, 2007 affirmance of the district court's decision in favor of our indirect subsidiary Irwin Mortgage Corporation (formerly Inland Mortgage Corporation). This lawsuit was filed in April 1996 in the United States District Court for the Northern District of Alabama, seeking class action status and alleging Irwin Mortgage's payment of broker fees to mortgage brokers violated the federal Real Estate Settlement Procedures Act. In its July 2, 2007 decision affirming summary judgment in favor of Irwin Mortgage, the court of appeals held that plaintiffs had failed to show that the total compensation Irwin Mortgage paid to the mortgage brokers was unreasonable in light of the services provided. The court of appeals also held that the district court had not abused its discretion in decertifying the plaintiffs' class because individual issues predominated, making class certification inappropriate. The plaintiffs have until May 29, 2008 to file a petition for a writ of certiorari seeking discretionary review by the United States Supreme Court. This action will conclude if a petition for certiorari is not filed, or is denied. We have not established any reserves for this case.

Table of Contents

Cohens v. Inland Mortgage Corporation

In October 2003, our indirect subsidiary, Irwin 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, alleged they were injured from lead contamination while living in premises allegedly owned by the defendants. The suit sought approximately \$41 million in damages and alleged negligence, breach of implied warranty of habitability and fitness for intended use, loss of services and the cost of medical treatment. On February 1, 2008, the parties agreed in principle to settle this case for a nonmaterial amount, subject to approval by the court.

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 class 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. On September 9, 2005, the *Kossler* plaintiffs filed a Third Amended Class Action Complaint. On October 21, 2005, Irwin filed a renewed motion seeking to dismiss the *Kossler* action.

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 September 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

Table of Contents

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. On September 17, 2004, Irwin made a demand for indemnification and a defense to *Hobson, Chatfield* and *Ransom*. Community denied this request as premature.

In response to a motion by Irwin, the Judicial Panel On Multidistrict Litigation consolidated *Hobson, Chatfield* and *Ransom* with *Kessler* in the Western District of Pennsylvania for all pretrial proceedings. The Pennsylvania District Court had been handling another case seeking class action status, *Kessler v. RFC, et al.*, also involving Community and with facts similar to those alleged in the Irwin consolidated cases. The *Kessler* case had been settled, but the settlement was appealed and set aside on procedural grounds. Subsequently, the parties in *Kessler* filed a motion for approval of a modified settlement, which would provide additional relief to the settlement class. Irwin is not a party to the *Kessler* action, but the resolution of issues in *Kessler* may have an impact on the Irwin cases. The Pennsylvania District Court has effectively stayed action on the Irwin cases until issues in the *Kessler* case are resolved. On January 25, 2008, the Pennsylvania District Court approved and certified for settlement purposes the modified *Kessler* settlement, finding the proposed modified *Kessler* settlement to be fair and reasonable, and directed the parties to supply a proposed notice plan. We have established an immaterial reserve for the Community litigation based upon SFAS 5 guidance and the advice of legal counsel.

Putkowski v. Irwin Home Equity Corporation and Irwin Union Bank and Trust Company

On August 12, 2005, our indirect subsidiary, Irwin Home Equity Corporation, and our direct subsidiary, Irwin Union Bank and Trust Company (collectively, Irwin), were named as defendants in litigation seeking class action status in the United States District Court for the Northern District of California for alleged violations of the Fair Credit Reporting Act. In response to Irwin's motion to dismiss filed on October 18, 2005, the court dismissed the plaintiffs' complaint with prejudice on March 23, 2006. Plaintiffs filed an appeal in the U.S. Court of Appeals for the 9th Circuit on April 13, 2006. On January 25, 2008, the parties agreed in principle to settle this litigation for a nonmaterial amount.

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.

Note 14 Financial Instruments With Off-Balance Sheet Risk

In the normal course of our business as a provider of financial services, we are party to certain financial instruments with off-balance sheet risk to meet the financial needs of our customers. These financial instruments include loan commitments and standby letters of credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized on the consolidated balance sheet. We follow the same credit policies in making commitments and contractual obligations as we do for our on-balance sheet instruments.

Our exposure to credit loss, in the form of nonperformance by the counterparty on commitments to extend credit and standby letters of credit, is represented by the contractual amount of those instruments. Collateral pledged for standby letters of credit and commitments varies but may include accounts receivable; inventory; property, plant, and equipment; and residential real estate. Total outstanding commitments to extend credit at December 31, 2007 and 2006 were \$1.1 billion and \$1.0 billion, respectively. These loan commitments include \$0.7 billion of

Table of Contents

floating rate loan commitments and \$0.4 billion of fixed rate loan commitments. We had approximately \$22 million and \$25 million in irrevocable standby letters of credit outstanding at December 31, 2007 and 2006, respectively.

Note 15 Derivative Financial Instruments

Financial derivatives are used as part of the overall asset/liability risk management process. We use certain derivative instruments that qualify and certain derivative instruments that do not qualify for hedge accounting treatment under SFAS 133. The derivatives that do not qualify for hedge treatment are classified as other assets and other liabilities and marked to market on the income statement. While we do not seek hedge accounting treatment for the assets and liabilities that these instruments are hedging, the economic purpose of these instruments is to manage the risk inherent in existing exposures to either interest rate risk or foreign currency risk.

During 2007, we entered into interest rate swaps to hedge floating rate deposits that have a notional amount of at December 31, 2007 of \$40 million that qualify for SFAS 133 hedge accounting treatment and interest rate swaps that have a notional amount of \$35 million that no longer qualify for SFAS 133 hedge accounting treatment. Under the terms of these swap agreements, we pay a fixed rate of interest and receive a floating rate of interest based on the Federal Funds rate. The total amount of loss on these swaps recorded to other comprehensive income at December 31, 2007 was \$1.2 million. Ineffectiveness related to the SFAS 133 cash flow hedges in 2007 was \$0.2 million. We recognized a loss of \$1.8 million for the year ended December 31, 2007 related to the swaps no longer qualifying for SFAS 133 treatment.

We have an interest rate swap that qualifies for hedge accounting treatment under SFAS 133 as a cash flow hedge in which we pay a fixed rate of interest and receive a floating rate. The purpose of this swap is to manage interest rate risk exposure created by Capital Trust XI which has variable rate interest payments. This hedge had a notional amount of \$15 million at December 31, 2007. The amount of loss on this swap recorded to other comprehensive income at December 31, 2007 and 2006 was \$0.3 million and \$0.1 million, respectively. A gain of \$0.1 million was recorded in interest expense related to this cash flow hedge in both 2007 and 2006, respectively. Ineffectiveness in 2007 and 2006 related to this cash flow hedge was immaterial.

In our home equity business, we have a \$10 million amortizing interest rate swap in which we pay a fixed rate of interest and receive a floating rate. The purpose of the swap is to manage interest rate risk exposure created by the 2005-1 securitization in which floating rate notes are funding fixed rate home equity loans. This swap is accounted for as a cash flow hedge in accordance with SFAS 133, with the changes in the fair value of the effective portion of the hedge reported as a component of equity. The net amount of gain or loss on these swaps recorded to other comprehensive income at December 31, 2007 and 2006 was \$8 thousand loss and \$0.3 million gain, respectively. A net gain of \$0.2 million, \$0.6 million and \$0.1 million was recorded in interest expense during the years ended December 31, 2007, 2006, and 2005, respectively, related to this cash flow hedge. Ineffectiveness related to this cash flow hedge in 2007, 2006, and 2005 was immaterial.

Also in our home equity business we utilize interest rate caps to mitigate the interest rate exposure created by the 2006-1, 2006-2, 2006-3 and 2007-1 securitizations in which floating rate notes are funding fixed rate home equity loans. We have \$165 million in amortizing interest rate caps relating to these hedging activities. These contracts are marked-to-market with gains and losses included in derivative gains (losses) on the consolidated income statements. We do not receive SFAS 133 hedge accounting treatment for these transactions. The gain (loss) on these activities for the years ended December 31, 2007 and 2006, totaled a loss of (\$0.2) million and \$3.0 million gain, respectively.

We enter into commitments to originate home equity loans whereby the interest rate on the loan is determined prior to funding (rate lock commitments). Rate lock commitments on loans intended to be sold are considered to be derivatives. We record changes in the fair value of these commitments based upon the current secondary market value

of securities with similar characteristics. For the years ended December 31, 2007, 2006, and 2005, a gain of \$0.1 million, a loss of \$0.1 million, and a gain of \$0.7 million was recorded in Gain from sale of loans. At December 31, 2007 and 2006, we had rate lock commitments outstanding totaling \$11 million and \$46 million.

We deliver Canadian dollar fixed rate leases into a commercial paper conduit. To lessen the repricing mismatch between fixed rate Canadian (CAD)-denominated leases and floating rate CAD-denominated commercial paper, a

Table of Contents

series of amortizing CAD interest rate swaps have been executed. As of December 31, 2007, the commercial paper conduit was providing \$194 million of variable rate funding. In total, our interest rate swaps were effectively converting \$192 million of this funding to a fixed interest rate. The losses on these swaps for the year ended December 31, 2007, 2006, and 2005 were \$0.5 million, \$0.3 million, and \$0.9 million, respectively.

We own foreign currency forward contracts to protect the U.S. dollar value of intercompany loans made to Irwin Commercial Finance Canada Corporation that are denominated in Canadian dollars. We had a contractual amount of \$108 million in forward contracts outstanding as of December 31, 2007. For the years ended December 31, 2007 and 2006, and 2005 we recognized a loss of \$6.9 million, a gain of \$1.4 million, and a loss of \$1.3 million, respectively. These contracts are marked-to-market with gains and losses included in derivative gains (losses) on the consolidated income statements. We do not receive SFAS 133 hedge accounting treatment for this transaction. For the years ended December 31, 2007, 2006, and 2005 we recognized a foreign currency transaction gain on the intercompany loans of \$7.7 million, a loss of \$0.6 million, and a gain of \$1.6 million, in each year respectively.

Note 16 Guarantees

Upon the occurrence of certain events under financial guarantees, we have performance obligations provided in certain contractual arrangements. These various agreements are summarized below.

We have sold loans and commercial loan participation interests to: (i) private investors; (ii) agency investors including, but not limited to, Federal National Mortgage Association (FNMA), Federal Home Loan Mortgage Corporation (FHLMC), and Government National Mortgage Association (GNMA); and (iii) other financial institutions. Each loan sale is subject to certain terms and conditions, which generally require us to indemnify and hold the investor harmless against any loss arising from errors and omissions in the origination, processing and/or underwriting of the loans. We are subject to this risk for loans that we originate as well as loans we acquire from brokers and correspondents. At December 31, 2007 and 2006, we had approximately \$23 million and \$13 million, respectively, recorded as an estimate for losses that may occur as a result of the guarantees described above based on trends in repurchase and indemnification requests, actual loss experience, known and inherent risks in the loans, and current economic conditions. The length of the indemnification period, which varies by investor and the nature of the potential defect may extend to the life of the loan. Because the extent of our obligations under these guarantees depends entirely on future events, our potential future liability under these agreements is not fully determinable.

We sell home equity loans to private investors. We have agreed to repurchase loans that do not perform at agreed-upon levels. The repurchase period generally ranges from 60-180 days after the settlement date. In addition, a repurchase obligation may be triggered if a loan does not meet specified representations related to credit information, loan documentation and collateral. At December 31, 2007 and 2006, respectively, we had approximately \$0.6 million and \$1.0 million recorded as an estimate for losses that may occur as a result of the guarantees described above based on trends in repurchase and indemnification requests, actual loss experience, known and inherent risks in the loans, and current economic conditions. Total home equity loans sold for which these guarantees apply were \$0.2 billion in 2007 and \$0.4 billion in 2006.

In the normal course of our servicing duties, we are often required to advance payments to investors, taxing authorities and insurance companies that are due and have not been received from borrowers as of specified cut-off dates. These servicing advances totaled \$11 million at December 31, 2007 and \$7 million at December 31, 2006 and are reflected as accounts receivable in the consolidated balance sheets. Servicing advances, including contractual interest, are considered a priority cash flow in the event of foreclosure or liquidation, thus making their collection more likely. At December 31, 2007 and 2006, we do not expect to incur any material losses and have not recorded any estimate of losses.

We provide guarantees to third parties on behalf of one of our subsidiaries related to operating lease payments with maturity dates extending through 2011. The maximum potential future payments guaranteed by us under these arrangements is \$10 million at December 31, 2007.

Table of Contents

We provide an operating performance guarantee to a third party on behalf of one of our subsidiaries related to borrowings to fund Canadian leases. At December 31, 2007 and 2006, our subsidiary had borrowings totaling \$192 million and \$180 million, respectively, for which our guarantee applied. Irwin Union Bank and Trust provides a credit guarantee up to \$25 million to a third party on behalf of one of our subsidiaries related to borrowings to fund Canadian leases. At December 31, 2007 and 2006, our subsidiary had borrowings totaling \$46 million and \$31 million, respectively, for which this guarantee applied.

Note 17 Regulatory Matters

Irwin Financial Corporation and its bank subsidiaries, Irwin Union Bank and Trust Company and Irwin Union Bank, F.S.B., are subject to various regulatory capital requirements administered by the federal and state banking agencies. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, Irwin Financial, Irwin Union Bank and Trust, and Irwin Union Bank, F.S.B. must meet specific capital guidelines that involve quantitative measures of their assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. Capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Failure to meet minimum capital requirements can elicit certain mandatory action by regulators that, if undertaken, could have direct material effect on our financial statements.

Quantitative measures established by regulation to ensure capital adequacy require minimum amounts and ratios (set forth in the following table) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and Tier I capital to average assets (as defined). We believe, as of December 31, 2007, that we have met all capital adequacy requirements to which we are subject, and met the regulatory definition of well-capitalized. In addition, we have established an internal Policy minimum capital ratio requirement of 11.0% (we have a higher Policy minimum of 12.0% at our principal subsidiary, Irwin Union Bank and Trust).

For an explanation of capital requirements and categories applicable to financial institutions, see the discussion in this Report in Part I, Item 1, Business, Supervision and Regulation, under the subsections Bank Holding Company Regulation Minimum Capital Requirements, and Bank and Thrift Regulation Capital Requirements, and Other Safety and Soundness Regulations.

Table of Contents

The following table presents actual capital amounts and ratios for Irwin Financial, Irwin Union Bank and Trust, and Irwin Union Bank, F.S.B. as compared to amounts and ratios required for Adequately and Well Capitalized status under the regulatory framework outlined by federal banking regulators:

	Actual		Adequately Capitalized		Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(Dollars in thousands)						
As of December 31, 2007						
Total Capital (to Risk-Weighted Assets):						
Irwin Financial Corporation	\$ 769,868	12.6%	\$ 487,936	8.0%	\$ 609,920	10.0%
Irwin Union Bank and Trust	683,999	12.5	437,404	8.0	546,755	10.0
Irwin Union Bank, F.S.B.	66,619	10.9	49,140	8.0	61,426	10.0
Tier I Capital (to Risk-Weighted Assets):						
Irwin Financial Corporation	619,656	10.2	243,968	4.0	365,952	6.0
Irwin Union Bank and Trust	584,393	10.7	218,702	4.0	328,053	6.0
Irwin Union Bank, F.S.B.	59,500	9.7	N/A		36,855	6.0
Tier I Capital (to Average Assets):						
Irwin Financial Corporation	619,656	10.2	244,192	4.0	305,240	5.0
Irwin Union Bank and Trust	584,393	10.6	221,323	4.0	276,654	5.0
Core Capital (to Adjusted Tangible Assets)						
Irwin Union Bank, F.S.B.	59,500	9.2	25,854	4.0	32,317	5.0
Tangible Capital (to Tangible Assets)						
Irwin Union Bank, F.S.B.	59,493	9.2	9,695	1.5	N/A	
As of December 31, 2006						
Total Capital (to Risk-Weighted Assets):						
Irwin Financial Corporation	\$ 837,754	13.4%	\$ 500,714	8.0%	\$ 625,893	10.0%
Irwin Union Bank and Trust	738,206	12.8	\$ 461,943	8.0	\$ 577,429	10.0
Irwin Union Bank, F.S.B.	59,157	11.3	\$ 42,028	8.0	\$ 52,535	10.0
Tier I Capital (to Risk-Weighted Assets):						
Irwin Financial Corporation	712,403	11.4	250,357	4.0	375,536	6.0
Irwin Union Bank and Trust	636,506	11.0	230,971	4.0	346,457	6.0
Irwin Union Bank, F.S.B.	55,820	10.6	N/A		31,521	6.0
Tier I Capital (to Average Assets):						
Irwin Financial Corporation	712,403	11.5	247,919	4.0	309,899	5.0
Irwin Union Bank and Trust	636,506	11.1	229,605	4.0	287,006	5.0
Core Capital (to Adjusted Tangible Assets)						
Irwin Union Bank, F.S.B.	55,820	11.1	20,162	4.0	25,203	5.0
Tangible Capital (to Tangible Assets)						
Irwin Union Bank, F.S.B.	55,804	11.1	7,516	1.5	N/A	

Note 18 Fair Values of Financial Instruments

Fair value estimates, methods and assumptions are set forth below for our financial instruments:

Cash and cash equivalents: The carrying amounts reported in the consolidated balance sheets for cash and cash equivalents approximate fair values.

Table of Contents

Interest-bearing deposits with financial institutions, Deposit liabilities, Other borrowings, and Long-term and collateralized debt: The fair values were estimated by discounting cash flows, using interest rates currently being offered for like assets and like liabilities with similar terms.

Loans and leases and loans held for sale: The fair values were estimated by discounting cash flows, using interest rates currently being offered for like assets with similar terms, to borrowers with similar credit quality, and for the same remaining maturities.

Residual interests: The carrying amounts reported in the consolidated balance sheets for residual interests approximate those assets' fair values. Fair value for residual interests is calculated using the methodologies specified in Note 1.

Servicing assets: Fair value for servicing assets is calculated using the methodologies specified in Note 1 and 7.

Investment securities: Fair values for investment securities were based on quoted market prices when available. For securities which had no quoted market prices, fair values were estimated by discounting future cash flows using current rates on similar securities. For FHLB and FRB stock, fair value is determined to be equal to cost as there is no readily determinable market value available for these securities.

Derivative instruments: The carrying amounts reported in the consolidated balance sheets for derivative instruments approximate those assets' fair values. The estimated fair values of derivative instruments are determined using third party statements.

Off-balance sheet loan commitments and standby letters of credit had an immaterial estimated fair value at December 31, 2007 and 2006. As of December 31, 2007 and 2006, our loan commitments had a contractual amount of \$1.1 billion and \$1.0 billion, respectively. Our standby letters of credit had a contractual amount of \$22 million and \$25 million at December 31, 2007 and 2006, respectively.

The estimated fair values of our financial instruments at December 31, were as follows:

	2007		2006	
	Carrying Amount	Estimated Fair Value (Dollars in thousands)	Carrying Amount	Estimated Fair Value
Financial assets:				
Cash and cash equivalents	\$ 78,212	\$ 78,212	\$ 145,765	\$ 145,765
Interest-bearing deposits with financial institutions	31,841	31,833	53,106	53,037
Residual interests	12,047	12,047	10,320	10,320
Investment securities	140,395	140,406	128,430	128,257
Loans held for sale	6,134	6,248	237,510	237,859
Loans and leases, net of unearned discount	5,696,230	5,746,148	5,238,193	5,259,341
Servicing asset	23,234	24,766	31,949	37,370
Derivatives	1,578	1,578	3,055	3,055
Assets held for sale	3,814	3,814	56,573	56,573
Financial liabilities:				

Edgar Filing: IRWIN FINANCIAL CORP - Form 10-K

Deposits	3,325,488	3,227,564	3,551,516	3,441,892
Other borrowings	802,424	812,751	602,443	604,590
Collateralized debt	1,213,139	1,226,835	1,173,012	1,156,032
Other long-term debt	233,873	235,261	233,889	237,271
Derivatives	5,065	5,065	612	612

The fair value estimates consider relevant market information when available. Because no market exists for a significant portion of our financial instruments, fair value estimates are determined based on present value of estimated cash flows and consider various factors, including current economic conditions and risk characteristics of

Table of Contents

certain financial instruments. Changes in factors, or the weight assumed for the various factors, could significantly affect the estimated values.

The fair value estimates are presented for existing on- and off-balance sheet financial instruments without attempting to estimate the value of our long-term relationships with depositors and the benefit that results from the low cost funding provided by deposit liabilities. In addition, significant assets that were not considered financial instruments and were therefore not a part of the fair value estimates include accounts receivable and premises and equipment.

Note 19 Equity Based Compensation

As of January 1, 2006, we adopted SFAS 123(R), Share-Based Payment, applying the modified prospective method. This statement requires all equity-based payments to employees, including grants of employee stock options, to be recognized as expense in the consolidated statement of income based on the grant date fair value of the award. Under the modified prospective method, we are required to record equity-based compensation expense for all awards granted after the date of adoption and for the unvested portion of previously granted awards outstanding as of the date of adoption. The fair values of stock options granted were determined using a Black-Scholes options-pricing model.

We have an employee stock purchase plan for all qualified employees. The plan provides for employees to purchase common stock through payroll deduction at approximately 85% of the current market value. For both of the years ended December 31, 2007 and 2006, \$0.1 million was expensed related to this plan.

We have a stock plan (established in 2001) that provides for the issuance of non-qualified and incentive stock options, stock appreciation rights, restricted stock, and phantom stock units.

We have issued restricted stock to compensate our Directors and employees with our common stock. The number of shares issued under these plans is based on the current market value of our common stock on date of issue. In 2007, we issued performance-based restricted stock whereby recipients vest after 3 years if pre-established performance criteria are achieved. For the year ended December 31, 2007 and 2006, \$0.8 million and \$0.4 million, respectively, was expensed related to these plans. The total fair value of shares vested during the years ended December 31, 2007, 2006, and 2005, was \$0.6 million, \$0.5 million, and \$0.1 million, respectively.

At December 31, 2007, there was \$2.2 million of total unrecognized compensation expense to be recognized over a weighted average period of 2.5 years related to restricted stock. Activity in these plans is summarized as follows:

	December 31, 2007	
	Number	Weighted
	of	Average Grant
	Shares	Date Fair Value
Unvested at the beginning of the year	84,681	\$ 21.04
Awarded	94,091	16.58
Vested	(28,434)	20.17
Forfeited	(10,077)	20.07
Unvested at the end of the year	140,261	\$ 18.30

We also issue stock options, which have a ten-year life and vest 25% at grant and 25% at each anniversary date thereafter. The exercise price is equal to the market price of our stock on the grant date. Compensation expense for these options is recognized on a straight-line basis over the vesting period. Outstanding stock options with exercise prices below the stock price have been considered as dilutive potential common shares in the computation of diluted earnings per share. During both of the years ended December 31, 2007 and 2006, \$1.7 million was expensed related to these plans. At December 31, 2007, there was \$1.5 million of total unrecognized compensation expense to be recognized over a weighted average period of 1.4 years related to unvested stock options. We received \$1.0 million in proceeds related to stock options exercised during the year and received a tax deduction of \$0.3 million related to these options.

Table of Contents

We calculated the fair value of each option award on the date of grant with the Black-Scholes option pricing model using certain key assumptions. The weighted-average fair value of each option granted during years ended December 31, 2007, 2006, and 2005 was \$5.21, \$5.60 and \$6.83, respectively. The total intrinsic value of options exercised during the years ended December 31, 2007, 2006 and 2005 was \$1.3 million, \$1.4 million and \$1.5 million, respectively. Expected life is estimated based on historical experience of employees' exercise behavior. Future expected volatility and dividend yield are primarily based on historical volatility and dividend yield levels. The risk-free rate is based on the U.S. Treasury rate with a maturity date corresponding to the options' expected life. The following assumptions were used for each respective period:

	For the Year Ended December 31,		
	2007	2006	2005
Risk-free interest rates	4.58%	4.92%	3.94%
Dividend yield	2.04%	2.40%	1.75%
Expected volatility	31%	32%	35%
Expected lives (in years)	6	6	6

The following table summarizes all stock option transactions under Company Plans during the year ended December 31, 2007:

	Number of Shares	2007		Aggregate Intrinsic Value as of 12/31/2007
		Weighted Average Exercise Price (In thousands)	Weighted Average Remaining Contractual Term	
Outstanding at the beginning of the year	2,445,795	\$ 20.44		
Granted	236,169	17.15		
Exercised	(67,603)	14.59		
Canceled	(114,304)	21.11		
Outstanding at the of the year	2,500,057	20.26	5.45	\$
Exercisable at the end of the year	2,066,740	\$ 20.69	4.80	\$

Table of Contents

In 2005 and in prior years, we used the intrinsic value method to account for our plans under the recognition and measurement principles of Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees, and related Interpretations. Therefore, except for costs related to restricted shares, we recognized no stock-based employee compensation cost in net income for any period prior to 2006, as all options granted under our plans had an exercise price equal to the market value of the underlying common stock on the date of grant.

	December 31, 2005 (Dollars in thousands, except per share amounts)
Net income from continuing operations as reported	\$ 36,247
Equity based compensation expense included in net earnings, net of tax	59
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(2,966)
Net income from continuing operations pro forma	33,340
Net (loss) income from discontinued operations	(17,260)
Pro forma net income	\$ 16,080
Basic earnings per share from continuing operations	
As reported	\$ 1.27
Pro forma	1.17
Basic earnings per share	
As reported	\$ 0.67
Pro forma	0.56
Diluted earnings per share continuing operations	
As reported	\$ 1.26
Pro forma	1.16
Diluted earnings per share	
As reported	\$ 0.66
Pro forma	0.56

Table of Contents**Note 20 Earnings Per Share**

Earnings per share calculations are summarized as follow:

	Net Loss	Preferred Dividends (In thousands, except per share amounts)	Basic Earnings Per Share	Effect of Stock Options	Diluted Earnings Per Share
Year ended December 31,					
2007					
Net loss allocable to common shareholders:					
From continuing operations	\$ (24,130)	(1,335)	(25,465)	(1,019)	\$ (26,484)
From discontinued operations	(30,543)		(30,543)		(30,543)
Total net loss from all operations	\$ (54,673)	(1,335)	(56,008)	(1,019)	\$ (57,027)
Shares			29,337	7	29,344
Per-share amount:					
For continuing operations			\$ (0.87)	(0.03)	\$ (0.90)
For all operations			\$ (1.91)	(0.03)	\$ (1.94)
2006					
Net income available to common shareholders:					
From continuing operations			\$ 37,401	(303)	\$ 37,098
From discontinued operations			(35,674)		(35,674)
Total net income from all operations			\$ 1,727	(303)	\$ 1,424
Shares			29,501	189	29,690
Per-share amount:					
For continuing operations			\$ 1.27	(0.02)	\$ 1.25
For all operations			\$ 0.06	(0.01)	\$ 0.05
2005					
Net income available to common shareholders:					
From continuing operations			\$ 36,247		\$ 36,247
From discontinued operations			(17,260)		(17,260)
Total net income from all operations			\$ 18,987		\$ 18,987
Shares			28,518	323	28,841
Per-share amount:					
For continuing operations			\$ 1.27	(0.01)	\$ 1.26

For all operations	\$	0.67	(0.01)	\$	0.66
--------------------	----	------	--------	----	------

In 2007, 2006 and 2005, there were 2.5 million, 1.9 million and 1.4 million shares, respectively, related to stock options that were not included in the dilutive earnings per share calculation because they had exercise prices above the stock price as of the respective dates. Also, the effect of convertible shares was not included in the 2005 diluted calculation because they were antidilutive.

Note 21 Income Taxes

In the U.S., the Corporation and our subsidiaries file and pay federal taxes as a consolidated entity. Our subsidiary, Irwin Commercial Finance Canada Corporation, (and related entities) files and pays taxes to certain Canadian revenue authorities.

Table of Contents

Our provision (benefit) for income taxes is based on analysis of our current and future tax liabilities. Income tax expense (benefit) is summarized as follows:

	2007	2006	2005
	(Dollars in thousands)		
Current:			
Federal	\$ 11,969	\$ 18,915	\$ 18,464
State	(2,067)	5,809	5,208
Foreign	3,832	1,695	1,287
	13,734	26,419	24,959
Deferred:			
Federal	(29,975)	(6,199)	(3,485)
State	(2,941)	(1,476)	(831)
Foreign	(1,666)	126	(48)
	(34,582)	(7,549)	(4,364)
Income tax expense:			
Federal	(18,006)	12,716	14,979
State	(5,008)	4,333	4,377
Foreign	2,166	1,821	1,239
	\$ (20,848)	\$ 18,870	\$ 20,595

A reconciliation of income tax expense (benefit) to the amount computed by applying the statutory income tax rate of 35% to income before income taxes is summarized as follows:

	2007	2006	2005
	(Dollars in thousands)		
Income taxes computed at the statutory rate	\$ (15,742)	\$ 19,695	\$ 19,895
Increase (decrease) resulting from:			
Nontaxable interest from investment securities and loans	(117)	(124)	(117)
Nontaxable income from bank owned life insurance	(707)		
State tax, net of federal benefit	(3,255)	2,816	2,845
Change in federal deferred tax resulting from tax rate change	(547)		
Foreign operations	(180)	(673)	183
Reserve adjustment ⁽¹⁾	87	(611)	(1,870)
Federal tax credits	(822)	(2,113)	(507)
Other items net	435	(120)	166
	\$ (20,848)	\$ 18,870	\$ 20,595

- (1) Tax reserves are adjusted as we align our tax liability to a level commensurate with our current identified tax exposures.

Table of Contents

Our net deferred tax asset (liability), which is included in other assets (other liabilities) on the consolidated balance sheet, consisted of the following:

	December 31,	
	2007	2006
	(Dollars in thousands)	
Deferred tax assets:		
Reserve for credit losses	\$ 74,995	\$ 37,728
Deferred compensation	2,614	1,601
Retirement benefits	4,140	2,427
Leasing	2,776	1,071
Mark to market	2,022	1,402
Capital loss carryforward ⁽¹⁾	4,513	3,511
Net operating loss carryforwards ⁽²⁾	3,560	
Other	7,509	5,629
	102,129	53,369
Deferred tax liabilities:		
Mortgage servicing	(7,712)	(11,513)
Deferred securitization income	(1,364)	
Deferred origination fees and costs	(7,123)	(5,688)
Other	(2,301)	(1,973)
	(18,500)	(19,174)
Net deferred tax asset ⁽³⁾	\$ 83,629	\$ 34,195

(1) As of December 31, 2007, we have \$4.5 million (after tax) of US capital loss carryforwards which expire in 2008 (\$0.2 million), 2010 (\$0.6 million), 2011 (\$2.4 million) and 2012 (\$1.3 million).

(2) As of December 31, 2007, we have \$3.6 million (after-tax) of US net operating loss carryforwards which expire in 2027.

(3) We have no valuation allowance recorded related to our net deferred tax asset at December 31, 2007 and 2006.

Effective January 1, 2007, we adopted FASB Interpretation 48, Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109, (FIN 48), which prescribes a single, comprehensive model for how a company should recognize, measure, present and disclose in its financial statements uncertain tax positions that the company has taken or expects to take on its tax returns. Upon adoption of FIN 48, we did not recognize any material adjustment in our liability for unrecognized tax benefits.

The following table summarizes the activity related to our unrecognized tax benefits, which relate primarily to U.S. federal temporary tax items.

	(Dollars in thousands)
Balance at January 1, 2007	\$ (10,695)
Increases related to prior year tax positions	(5,206)
Expiration of the statute of limitations	2,892
Balance at December 31, 2007	\$ (13,009)

As of January 1, 2007, our unrecognized tax benefits were \$10.7 million, \$0.7 million of which would, if recognized, favorably affect the effective tax rate in future periods. As of December 31, 2007, our unrecognized tax benefits were \$13.0 million, \$0.2 million of which would, if recognized, favorably affect the effective tax rate in future periods. We do not expect our unrecognized tax benefits to change significantly over the next 12 months.

Table of Contents

Our continuing practice is to recognize interest and penalties related to unrecognized tax benefits in income tax expense. As of January 1, 2007, we had approximately \$0.8 million accrued for interest and no accrual for penalties related to unrecognized tax benefits. As of December 31, 2007, we have approximately \$1.1 million accrued for interest related to unrecognized tax benefits and no accrual for penalties.

Tax years 2004-2006 remain open to examination by major taxing jurisdictions. Certain state tax returns remain open to examination for tax years 2003-2006.

Note 22 Employee Retirement Plans

We have contributory retirement and savings plans that cover all eligible employees and meet requirements of Section 401(k) of the Internal Revenue Code. Employees' contributions to the plan are matched 60% by us up to 5% of the employee's compensation up to a maximum match of \$6,750 in 2007.

The matching vests 20% each year over a period of 5 years. The expense to match employee contributions for the years ended December 31, 2007, 2006 and 2005 was \$2.2 million, \$1.6 million and \$1.8 million, respectively.

We have a defined benefit plan currently covering eligible employees of our commercial banking segment and the parent company. The benefits are based on years of service and the employee's compensation during their employment. Contributions are intended to provide not only for benefits attributed to service to date but also for those expected to be earned in the future.

IRS limits reduce the benefits that an executive officer can earn under the Employees' Pension Plan's basic formula. As a result, the Corporation provides an additional benefit under the Irwin Financial Corporation Restated Supplemental Executive Retirement Plan (the SERP). The SERP is provided to executive officers in order to make them whole for the benefits under the basic formula that could not be provided under the Employees' Pension Plan due to these limits. The SERP is not funded and is a general obligation of the Corporation.

The following table sets forth amounts recognized in our balance sheet for these benefit plans:

	Pension Benefits		SERP Benefits	
	December 31,		December 31,	
	2007	2006	2007	2006
	(Dollars in thousands)		(Dollars in thousands)	
Change in benefit obligation:				
Projected benefit obligation at January 1,	\$ 41,443	\$ 36,063	\$ 7,314	\$ 7,882
Service cost	4,054	3,723	104	235
Interest cost	2,425	2,077	313	377
Actuarial (gain) loss	(824)	459	(1,938)	(950)
Benefits paid	(942)	(879)	(229)	(230)
Benefit obligation at December 31,	46,156	41,443	5,564	7,314
Change in plan assets:				
Fair value plan assets at January 1,	31,934	28,699		
Actual return on plan assets	2,113	4,114		
Benefits paid	(942)	(879)	(229)	(230)

Employer contributions			229	230
Fair value plan assets at December 31,	33,105	31,934		
Funded status at December 31, (included in Other Liabilities)	\$ (13,051)	\$ (9,509)	\$ (5,564)	\$ (7,314)

Table of Contents

Net pension and SERP costs included the following components:

Employee pension plan

	2007	2006	2005
	(Dollars in thousands)		
Service cost	\$ 4,054	\$ 3,723	\$ 2,856
Interest cost	2,425	2,077	1,741
Expected return on plan assets	(2,507)	(2,252)	(1,912)
Amortization of prior service cost	37	37	37
Amortization of actuarial loss	545	871	687
Net pension cost	\$ 4,554	\$ 4,456	\$ 3,409

Supplemental Executive Retirement Plan

	2007	2006	2005
	(Dollars in thousands)		
Service cost	\$ 104	\$ 235	\$ 257
Interest cost	313	377	404
Transition obligation	11	11	11
Amortization of prior service cost	1	1	1
Amortization of actuarial loss		97	167
Net pension cost	\$ 429	\$ 721	\$ 840

To develop the expected long-term rate of return on plan assets assumption, we considered the historical returns and the future expectations for returns for each asset class, as well as the target asset allocation of the pension portfolio. This resulted in the selection of the 8.00% long-term rate of return on assets assumption listed below. The discount rate used in determining the benefit obligation is selected by reference to the year-end Moody's AA rate.

Pension Benefits		SERP Benefits	
Year Ending		Year Ending	
December 31,		December 31,	
2007	2006	2007	2006
(Dollars in thousands)		(Dollars in thousands)	

Amounts not yet reflected in net periodic benefit cost and included in accumulated other comprehensive income:

Transition obligation	\$	\$	\$	\$
Prior service cost	(199)	(236)	(33)	(34)

Edgar Filing: IRWIN FINANCIAL CORP - Form 10-K

Accumulated loss	(8,200)	(9,175)	(56)	(1,995)
Accumulated other comprehensive income	\$ (8,399)	\$ (9,411)	\$ (95)	\$ (2,045)
Net periodic benefit cost in excess of cumulative employer contributions	(4,652)	(98)	(5,469)	(5,269)
Net amount recognized in statement of financial position	\$ (13,051)	\$ (9,509)	\$ (5,564)	\$ (7,314)
Change in accumulated other comprehensive income				
Additional minimum liability	\$	\$ (541)	\$	\$
Intangible asset offset		236		
Accumulated other comprehensive income		(305)		
Net increase to accumulated other comprehensive income	\$ (8,399)	\$ (9,106)	\$ (95)	\$ (2,045)

Table of Contents**Weighted average assumptions:**

	Pension Benefits		SERP Benefits	
	Year Ending	Year Ending	Year Ending	Year Ending
	December 31,	December 31,	December 31,	December 31,
	2007	2006	2007	2006
To determine benefit obligations at December 31,				
Discount rate	6.00%	5.75%	6.00%	5.75%
Rate of average compensation increases	4.18	4.18	4.25	4.25
To Determine net periodic benefit cost at January 1,				
Discount rate	5.75%	5.50%	5.75%	5.50%
Expected rate of return on plan assets	8.00	8.00	N/A	N/A
Rate of average compensation increases	4.18	4.18	4.25	4.25
	December 31,	December 31,	December 31,	December 31,
	2007	2006	2007	2006
	(Dollars in thousands)		(Dollars in thousands)	
Projected benefit obligation	\$ 46,156	\$ 41,443	\$ 5,564	\$ 7,314
Accumulated benefit obligation	37,243	32,573	5,172	5,238
Fair value of assets	33,105	31,934		

The estimated prior service cost for the defined benefit pension plan and the supplement executive retirement plan (SERP) that will be amortized from accumulated other comprehensive income (AOCI) into net periodic benefit cost over the next fiscal year is \$46 thousand and \$1 thousand, respectively. The estimated net loss for the defined benefit pension plan and the expected transition obligation for the SERP plan that will be amortized from AOCI into net periodic benefit cost over the next fiscal year is \$322 thousand and 6 thousand, respectively.

Plan Assets

Our pension plan asset allocation at December 31, 2007, and 2006, and target allocation for 2008, by asset category are as follows:

Asset Category	Percentage of Plan Assets		Target Allocation 2008
	2007	2006	
Equity securities			
Domestic	50%	57%	30-50%
International	11	14	15-25
Fixed income securities	23	25	15-25
Cash equivalents	16	4	1-10
Alternative investments			10-20

100% 100%

Each mutual fund in which the portfolio invests will be reviewed on a quarterly basis and rebalanced back to the normal weighting if the actual weighting varies by 2% or more from the targeted weighting. The allocation of assets in the portfolio may deviate from target allocation when market conditions warrant. Such deviations are designed primarily to reduce overall investment risk in the long term. In addition, allocations may deviate from target shortly after cash contributions are made to the plan, but prior to the rebalancing of these portfolios.

The portfolio will be managed in a style-neutral manner that seeks to minimize principal fluctuations over the established time horizon and that is consistent with the portfolio's stated objectives. Over the long-term, the investment objectives for this portfolio shall be to achieve an average total annual rate of return that consists of the Consumer Price Index (CPI) plus 6% for the aggregate investments. Returns may vary significantly from this target year to year.

Table of Contents**Cash Flows**

We did not make a contribution to the pension plan in 2007 and do not currently plan to make a contribution in 2008.

Outflows from the pension plan are dependent on a number of factors, principally the retirement date; earnings at retirement; and the draw period for retirees. Our current estimated future benefit payments for the benefit plans are as follows (in thousands):

	Pension Benefits	SERP Benefits
Expected benefit payments (in thousands):		
2008	\$ 997	\$ 230
2009	1,202	224
2010	1,460	219
2011	1,693	238
2012	1,933	346
Years 2013-2017	12,950	1,700

Note 23 Industry Segment Information

We have three principal business segments that provide a broad range of banking products and services, including commercial banking, commercial finance, and consumer mortgage products and services.

As described in Note 2, we have recently exited the conforming, conventional mortgage banking line of business. This segment is shown in the table below as Discontinued Operations. Our other segment primarily includes the parent company, unsold portions of businesses in which we no longer engage, and eliminations.

The accounting policies of each segment are the same as those described in Note 1 Accounting Policies, Management Judgments and Accounting Estimates.

Table of Contents

	Consolidated							Consolidated
	Commercial Banking	Commercial Finance	Home Equity Lending	Other	Continuing Operations	Discontinued Operations		
	(Dollars in thousands)							
2007								
Net interest income	\$ 103,249	\$ 79,587	\$ 15,177	\$ (70,608)	\$ 127,405	\$ (1,826)	\$ 125,579	
Intersegment interest	(2,561)	(40,371)	(23,324)	66,256				
Other revenue	16,615	13,106	445	(2,782)	27,384	(15,364)	12,020	
Intersegment revenues			2,090	(2,090)				
Total net revenues	117,303	52,322	(5,612)	(9,224)	154,789	(17,190)	137,599	
Other expense	88,954	28,492	70,786	11,535	199,767	33,934	233,701	
Intersegment expenses	3,652	1,615	2,646	(7,913)				
Income (loss) before taxes	24,697	22,215	(79,044)	(12,846)	(44,978)	(51,124)	(96,102)	
Income taxes	8,844	8,659	(31,593)	(6,758)	(20,848)	(20,581)	(41,429)	
Net income (loss)	\$ 15,853	\$ 13,556	\$ (47,451)	\$ (6,088)	\$ (24,130)	\$ (30,543)	\$ (54,673)	
Assets at December 31,	\$ 3,093,764	\$ 1,302,688	\$ 1,481,306	\$ 288,347			\$ 6,166,105	
2006								
Net interest income	\$ 113,844	\$ 65,387	\$ 108,133	\$ (65,026)	\$ 222,338	\$ 23,698	\$ 246,036	
Intersegment interest	5,148	(29,543)	(34,724)	59,119				
Other revenue	18,173	8,018	14,738	3,692	44,621	14,285	58,906	
Intersegment revenues			448	(448)				
Total net revenues	137,165	43,862	88,595	(2,663)	266,959	37,983	304,942	
Other expense	86,170	22,838	83,035	18,645	210,688	97,489	308,177	
Intersegment expenses	2,762	1,117	2,932	(6,811)				
Income (loss) before taxes	48,233	19,907	2,628	(14,497)	56,271	(59,506)	(3,235)	
Income taxes	17,373	7,307	1,090	(6,900)	18,870	(23,832)	(4,962)	
Net income (loss)	\$ 30,860	\$ 12,600	\$ 1,538	\$ (7,597)	\$ 37,401	\$ (35,674)	\$ 1,727	
Assets at December 31,	\$ 3,103,547	\$ 1,073,552	\$ 1,617,219	\$ 443,640			\$ 6,237,958	
2005								
Net interest income	\$ 95,131	\$ 29,392	\$ 104,645	\$ (25,008)	\$ 204,160	\$ 34,878	\$ 239,038	
Intersegment interest	10,341	(1,920)	(32,166)	23,745				
Other revenue	16,686	7,437	33,667	(1,069)	56,721	63,765	120,486	
Intersegment revenues	259			(259)				

Edgar Filing: IRWIN FINANCIAL CORP - Form 10-K

Total net revenues	122,417	34,909	106,146	(2,591)	260,881	98,643	359,524
Other expense	75,347	21,453	99,119	8,120	204,039	127,516	331,555
Intersegment expenses	1,715	771	3,220	(5,706)			
Income (loss) before taxes	45,355	12,685	3,807	(5,005)	56,842	(28,873)	27,969
Income taxes	17,976	5,252	1,555	(4,188)	20,595	(11,613)	8,982
Net income (loss)	\$ 27,379	\$ 7,433	\$ 2,252	\$ (817)	\$ 36,247	\$ (17,260)	\$ 18,987
Assets at December 31,	\$ 3,162,398	\$ 831,657	\$ 1,602,400	\$ 1,050,069			\$ 6,646,524

Table of Contents**Note 24 Irwin Financial Corporation (Parent Only) Financial Information**

The condensed financial statements of the parent company as of December 31, 2007 and 2006, and for the three years ended December 31, 2007 are presented below:

Condensed Balance Sheets

	December 31,	
	2007	2006
	(Dollars in thousands)	
Assets:		
Cash and short-term investments	\$ 1,227	\$ 839
Investment in bank subsidiaries	639,854	689,654
Investments in non-bank subsidiaries	3,385	3,793
Loans to bank subsidiaries	42,497	64,618
Other assets	27,809	10,953
	\$ 714,772	\$ 769,857
Liabilities:		
Long-term debt	\$ 233,868	\$ 233,868
Other liabilities	21,604	5,487
	255,472	239,355
Shareholders equity:		
Perpetual Preferred Stock	14,441	14,518
Common stock	116,542	116,192
Other shareholders equity	328,317	399,792
	459,300	530,502
	\$ 714,772	\$ 769,857

Table of Contents**Condensed Statements of Income**

	For the Year Ended December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Income:			
Dividends from non-bank subsidiaries	\$ 951	\$ 348	\$ 1,417
Dividends from bank subsidiary	15,000	15,000	50,000
Interest income	3,569	3,443	4,218
Other	14,846	11,249	15,615
	34,366	30,040	71,250
Expenses:			
Interest expense	17,302	20,082	23,983
Salaries and benefits	13,705	11,416	9,973
Other	4,991	5,754	6,191
	35,998	37,252	40,147
(Loss) income before income taxes and equity in undistributed income of subsidiaries	(1,632)	(7,212)	31,103
Income tax benefit, less amounts charged to subsidiaries	(6,063)	(10,230)	(9,900)
	4,431	3,018	41,003
Equity in undistributed income (loss) of subsidiaries	(59,104)	(1,291)	(22,016)
Net (loss) income	\$ (54,673)	\$ 1,727	\$ 18,987

Table of Contents**Condensed Statements of Cash Flows**

	For the Year Ended December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Net (loss) income	\$ (54,673)	\$ 1,727	\$ 18,987
Adjustments to reconcile net (loss) income to cash provided by operating activities:			
Equity in undistributed income (loss) of subsidiaries	59,104	1,291	22,016
Depreciation and amortization	363	2,853	2,652
Decrease in taxes payable	(4,484)	(8,800)	(11,442)
Decrease (increase) in interest receivable	46	(25)	661
Decrease in interest payable		(506)	(176)
Net change in other assets and other liabilities	4,745	14,600	(8,847)
Net cash provided by operating activities	5,101	11,140	23,851
Lending and investing activities:			
Net decrease (increase) in loans to subsidiaries	22,120	1,022	(2,289)
Investments in subsidiaries	(3,500)		(5,081)
Net sales (purchases) of premises and equipment	251	(339)	15
Net cash provided (used) by lending and investing activities	18,871	683	(7,355)
Financing activities:			
Net decrease in borrowings			(9,024)
Proceeds from long-term debt		61,500	51,750
Payments of long-term debt		(77,509)	(51,750)
Proceeds from the sale of noncumulative perpetual preferred stock	(77)	14,518	
Purchase of treasury stock	(12,804)	(4,363)	(1,201)
Proceeds from sale of stock for employee benefit plans	2,085	7,740	3,277
Dividends paid	(15,381)	(13,110)	(11,426)
Net cash used by financing activities	(26,177)	(11,224)	(18,374)
Net (decrease) increase in cash and cash equivalents	(2,205)	599	(1,878)
Effect of exchange rate changes on cash	2,593	(44)	1,051
Cash and cash equivalents at beginning of year	839	284	1,111
Cash and cash equivalents at end of year	\$ 1,227	\$ 839	\$ 284
Supplemental disclosures of cash flow information:			
Cash paid during the year:			
Interest	\$ 17,302	\$ 20,588	\$ 24,159
Income tax payments	\$ 10,362	\$ 92,783	\$ 14,920

Non cash transactions:

Adoption of FAS 156	\$ 2,905	\$	\$
Conversion of trust preferred to common stock	\$	\$ 20,248	\$

Table of Contents**Note 25 Summary of Quarterly Financial Information (Unaudited)**

	2007			
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
	(Dollars in thousands)			
Summary Income Information				
Interest Income	\$ 127,463	\$ 129,850	\$ 128,678	\$ 127,038
Interest expense	(62,187)	(64,704)	(62,834)	(60,910)
Provision for loan and lease losses	(63,832)	(28,493)	(19,454)	(23,208)
Other income	11,584	7,032	9,581	(814)
Other expense	(54,074)	(46,345)	(47,064)	(52,285)
Provision for income taxes	18,341	1,857	(3,436)	4,085
Net (loss) income from continuing operations	\$ (22,705)	\$ (803)	\$ 5,471	\$ (6,094)
Net loss from discontinued operations	\$ (3,420)	\$ (17,227)	\$ (5,860)	\$ (4,035)
Net (loss) income	\$ (26,125)	\$ (18,030)	\$ (389)	\$ (10,129)
Earnings per share of common stock from continuing operations:				
Basic ⁽¹⁾	\$ (0.79)	\$ (0.04)	\$ 0.18	\$ (0.22)
Diluted ⁽¹⁾	(0.80)	(0.05)	0.17	(0.22)
Earnings (loss) per share of common stock:				
Basic ⁽¹⁾	\$ (0.91)	\$ (0.63)	\$ (0.02)	\$ (0.35)
Diluted ⁽¹⁾	(0.92)	(0.64)	(0.03)	(0.36)

	2006			
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
	(Dollars in thousands)			
Summary Income Information				
Interest Income	\$ 129,264	\$ 123,788	\$ 117,609	\$ 111,467
Interest expense	(62,571)	(58,491)	(53,737)	(49,889)
Provision for loan and lease losses	(9,946)	(9,135)	(6,826)	(9,193)
Other income	14,232	7,347	9,046	13,996
Other expense	(55,717)	(50,864)	(51,295)	(52,814)
Provision for income taxes	(4,615)	(3,550)	(5,828)	(4,877)
Net income from continuing operations	\$ 10,647	\$ 9,095	\$ 8,969	\$ 8,690
Net (loss) income from discontinued operations	\$ (5,726)	\$ (13,302)	\$ (6,098)	\$ (10,548)
Net income (loss)	\$ 4,921	\$ (4,207)	\$ 2,871	\$ (1,858)

Earnings per share of common stock from continuing operations:

Basic ⁽¹⁾	\$	0.36	\$	0.31	\$	0.30	\$	0.30
Diluted ⁽¹⁾		0.35		0.30		0.30		0.30
Earnings (loss) per share of common stock:								
Basic ⁽¹⁾	\$	0.17	\$	(0.14)	\$	0.10	\$	(0.06)
Diluted ⁽¹⁾		0.16		(0.14)		0.09		(0.07)

(1) Our quarterly earnings per share are based on actual quarterly data and may not add up exactly to year-to-date earnings per share due to rounding and the impact of antidilutive shares.

Table of Contents

Item 9. *Changes in and Disagreements with Accountants on Accounting and Financial Disclosure*

Not applicable

Item 9A. *Controls and Procedures.*

Evaluation of Disclosure Controls and Procedures

Disclosure Controls and Procedures As of the end of the period covered by this report, the Corporation carried out an evaluation as required by Rule 13a-15(b) or 15d-15(b) of the Securities Exchange Act of 1934 (Exchange Act), under the supervision and with the participation of management, including the Chief Executive Officer (CEO) and the Chief Financial Officer (CFO), of the effectiveness of the Corporation s disclosure controls and procedures as defined in Exchange Act Rule 13a-15(e) or 15d-15(e). Based on this evaluation, the CEO and the CFO have concluded that the Corporation s disclosure controls and procedures were effective as of December 31, 2007.

Management s Report on Internal Control Over Financial Reporting

See Management s Report on Internal Control over Financial Reporting in Item 8, which is incorporated herein by reference.

Changes in Internal Control Over Financial Reporting

Internal Control Over Financial Reporting In connection with the evaluation performed by management with the participation of the CEO and the CFO as required by Exchange Act Rule 13a-15(d) or 15d-15(d), there were no changes in the Corporation s internal control over financial reporting as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) that occurred during the year ended December 31, 2007 that have materially affected, or are reasonably likely to materially affect, the Corporation s internal control over financial reporting.

Item 9B. *Other Information*

Not applicable

Table of Contents

PART III

Item 10. *Directors, Executive Officers and Corporate Governance.*

The information contained in our proxy statement for the 2008 Annual Meeting of Shareholders in the sections entitled Section 16(a) Beneficial Ownership Reporting Compliance, Director Nominees, Current Directors, and Audit Committee is incorporated herein by reference in response to this item. See also the section entitled Executive Officers in Part I, Item 1, Business of this Report on Form 10-K.

The following documents are posted on the Corporate Governance section of our website at www.irwinfinancial.com:

Our Code of Conduct (our code of business conduct and ethics), which is applicable to our directors, officers, and employees, including our Chief Executive Officer (principal executive officer), our Chief Financial Officer (principal financial officer) and our Controller (principal accounting officer). Our Code of Conduct is filed as Exhibit 14.1 to this Report on Form 10-K. Amendments to or waivers for executive officers or directors from our Code of Conduct will be posted on our website.

Our Governance (nominating) Committee Charter.

Our Compensation Committee Charter.

Our Audit Committee Charter, which is Appendix A to our Proxy Statement.

Our Risk Committee Charter.

Our Executive Committee Charter.

The Code of Conduct and the above-mentioned charters, together with our Corporate Governance Principles (corporate governance guidelines), are available in paper or e-mail copy to any shareholder who makes a request in writing to: Sue Elliott, Finance Department, Irwin Financial Corporation, 500 Washington Street, Columbus, IN 47201, or via e-mail at info@irwinfinancial.com.

Item 11. *Executive Compensation.*

The information contained in our proxy statement for the 2008 Annual Meeting of Shareholders in the section entitled Compensation is incorporated herein by reference in response to this item.

Item 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.*

The information contained in our proxy statement for the 2008 Annual Meeting of Shareholders in the section entitled Principal Holders of Irwin Financial Securities, Securities Ownership of Directors and Management, Securities Authorized for Issuance Under Equity Compensation Plans, is incorporated herein by reference in response to this item.

Item 13. *Certain Relationships and Related Transactions, and Director Independence.*

The information contained in our proxy statement for the 2008 Annual Meeting of Shareholders in the sections entitled Transactions with Related Persons and Director Independence is incorporated herein by reference in response to this item.

Item 14. *Principal Accountant Fees and Services.*

The information contained in our proxy statement for the 2008 Annual Meeting of Shareholders in the sections entitled Auditor Fees, and Pre-approval of Services Rendered by Independent Auditors is incorporated herein by reference in response to this item.

Table of Contents

PART IV

Item 15. *Exhibits and Financial Statement Schedules.*

(a) Documents filed as part of this report.

1. Financial Statements

Management Report on Responsibility for Financial Reporting

Report of Independent Registered Public Accounting Firm

Irwin Financial Corporation and Subsidiaries

Consolidated Balance Sheets for the years ended 2007 and 2006

Consolidated Statements of Income for the years ended 2007, 2006 and 2005

Consolidated Statements of Changes in Shareholders' Equity for the years ended 2007, 2006, and 2005

Consolidated Statements of Cash Flows for the years ended 2007, 2006, and 2005

Notes to Consolidated Financial Statements

2. Financial Statement Schedules

None

3. Exhibits to Form 10-K

**Exhibit
Number**

Description of Exhibit

- | | |
|-----|---|
| 2.1 | Asset Purchase Agreement by and among Irwin Financial Corporation, Irwin Mortgage Corporation and Freedom Mortgage Corporation dated as of August 7, 2006. (Incorporated by reference to Exhibits 2.1 and 2.2 of Form 8-K filed October 2, 2006, File No. 001-16691.) |
| 3.1 | Restated Articles of Incorporation of Irwin Financial Corporation, as amended December 20, 2006. (Incorporated by reference to Exhibit 3.1 of Form 10-K for period ended December 31, 2006, and filed March 9, 2007, File No. 001-16691.) |
| 3.2 | Code of By-laws of Irwin Financial Corporation, as amended, February 15, 2007. (Incorporated by reference to Exhibit 3.2 of Form 10-K filed March 9, 2007, File No. 001-16691.) |
| 3.3 | Code of By-laws of Irwin Financial Corporation, as amended November 28, 2007. (Incorporated by reference to Exhibit 3.1 of Form 8-K filed November 30, 2008.) |
| 4.1 | Specimen Common Stock Certificate. (Incorporated by reference to Exhibit 4.1 of Form 10-K filed March 9, 2007, File No. 001-16691.) |
| 4.2 | |

Certain instruments defining the rights of the holders of long-term debt of Irwin Financial Corporation and certain of its subsidiaries, none of which authorize a total amount of indebtedness in excess of 10% of the total assets of the Corporation and its subsidiaries on a consolidated basis, have not been filed as Exhibits. The Corporation hereby agrees to furnish a copy of any of these agreements to the Commission upon request

- 4.3 Rights Agreement, dated as of March 1, 2001, between Irwin Financial Corporation and Irwin Union Bank and Trust. (Incorporated by reference to Exhibit 4.1 to Form 8-A filed March 2, 2001, File No. 000-06835.)
- 4.4 Appointment of Successor Rights Agent dated as of May 11, 2001 between Irwin Financial Corporation and National City Bank. (Incorporated by reference to Exhibit 4.5 to Form S-8 filed on September 7, 2001, File No. 333-69156.)
- 10.1 *Irwin Financial Corporation 1997 Stock Option Plan. (Incorporated by reference to Exhibit 10 to Form 10-Q Report for quarter ended June 30, 1997, and filed August 12, 1997, File No. 000-06835.)

Table of Contents

Exhibit Number	Description of Exhibit
10.2	*Amendment Number One to Irwin Financial Corporation 1997 Stock Option Plan. (Incorporated by reference to Exhibit 10(l) to Form 10-K405 Report for the period ended December 31, 1997, filed March 30, 1998, File No. 000-06835.)
10.3	*Irwin Union Bank and Trust Company Business Development Board Compensation Program. (Incorporated by reference to Form S-8 filed on July 19, 2000, File No. 333-41740.)
10.4	*Irwin Union Bank and Trust Company Business Development Board Compensation Program as amended November 28, 2006.
10.5	*Irwin Financial Corporation Amended and Restated 2001 Stock Plan, as amended and restated May 10, 2007. (Incorporated by reference to Exhibit 99.1 of Form 8-K filed May 16, 2007, File No. 001-16691.)
10.6	*Amendment Number One to the Irwin Financial Corporation Amended and Restated 2001 Stock Plan. (Incorporated by reference to Exhibit 10.1 of Form 8-K filed February 11, 2008, File No. 001-16691.)
10.7	*Irwin Financial Corporation 2001 Stock Plan Form of Stock Option Agreement and Notice of Stock Option Grant. (Incorporated by reference to Exhibit 99.1 of the Corporation's 8-K Current Report, filed May 9, 2005, File No. 001-16691.)
10.8	*Irwin Financial Corporation 2001 Stock Plan Form of Restricted Stock Agreement and Notice of Restricted Stock Award. (Incorporated by reference to Exhibit 99.2 of the Corporation's 8-K Current Report, filed May 9, 2005, File No. 001-16691.)
10.9	*Irwin Financial Corporation 2001 Stock Plan Form of Stock Option Agreement (Canada) (Incorporated by reference to Exhibit 10.8 of the Corporation's 10-Q Report for the quarter ended September 30, 2005, File No. 001-16691.)
10.10	*Irwin Financial Corporation 2001 Stock Plan Form of Restricted Stock Agreement (with Performance Criteria) and Notice of Restricted Stock Award with Performance Criteria. (Incorporated by reference to Exhibit 99.2 of Form 8-K, filed May 16, 2007, File No. 001-16691.)
10.11	*Irwin Financial Corporation 2001 Stock Plan Form of Restricted Stock Unit Agreement (with Performance Criteria) and Notice of Restricted Stock Unit Award with Performance Criteria. (Incorporated by reference to Exhibit 10.2 of Form 8-K, filed February 11, 2008, File No. 001-16691.)
10.12	*Irwin Financial Corporation 2001 Stock Plan Form of Restricted Stock Unit Agreement (No Performance Criteria) and Notice of Restricted Stock Unit Award.
10.13	*Irwin Financial Corporation 1999 Outside Director Restricted Stock Compensation Plan. (Incorporated by reference to Exhibit 2 of the Corporation's 2004 Proxy Statement for the Annual Meeting of Shareholders, filed March 18, 2004, File No. 001-16691.)
10.14	*Employee Stock Purchase Plan III. (Incorporated by reference to Exhibit 10(a) to Form 10-Q Report for the quarter ended June 30, 1999, File No. 000-06835.)
10.15	*Long-Term Management Performance Plan. (Incorporated by reference to Exhibit 10(a) to Form 10-K Report for the period ended December 31, 1986, File No. 000-06835.)
10.16	*Long-Term Incentive Plan-Summary of Terms. (Incorporated by reference to Exhibit 10(a) to Form 10-K Report for the period ended December 31, 1986, File No. 000-06835.)
10.17	*Amended and Restated Management Bonus Plan. (Incorporated by reference to Exhibit 10(a) to Form 10-K Report for the period ended December 31, 1986, File No. 000-06835.)
10.18	*Irwin Financial Corporation Amended and Restated Short Term Incentive Plan effective January 1, 2006. (Incorporated by reference to Exhibit 10.27 of Form 10-Q Report for the quarter ended June 30 2006, File No. 001-16691.)
10.19	*First Amendment to the Irwin Financial Corporation Amended and Restated Short Term Incentive Plan. (Incorporated by reference to Exhibit 10.28 of Form 10-Q Report for the quarter ended June 30 2007, File No. 001-16691.)

- 10.20 *Irwin Commercial Finance Amended and Restated Short Term Incentive Plan effective January 1, 2006. (Incorporated by reference to Exhibit 10.28 of Form 10-Q for the quarter ended June 30, 2006, File No. 001-16691.)

Table of Contents

Exhibit Number	Description of Exhibit
10.21	*First Amendment to the Irwin Commercial Finance Amended and Restated Short Term Incentive Plan. (Incorporated by reference to Exhibit 10.30 of Form 10-Q for the quarter ended June 30, 2007, File No. 001-16691.)
10.22	*Irwin Home Equity Amended and Restated Short Term Incentive Plan effective January 1, 2006. (Incorporated by reference to Exhibit 10.29 of Form 10-Q for the quarter ended June 30, 2006, File No. 001-16691.)
10.23	*First Amendment to the Irwin Home Equity Amended and Restated Short Term Incentive Plan effective January 1, 2006. (Incorporated by reference to Exhibit 10.32 of Form 10-Q for the quarter ended June 30, 2007, File No. 001-16691.)
10.24	*Irwin Union Bank and Trust Company Amended and Restated Short Term Incentive Plan effective January 1, 2006. (Incorporated by reference to Exhibit 10.31 of Form 10-Q Report for the quarter ended June 30, 2006, File No. 001-16691.)
10.25	*First Amendment to the Irwin Union Bank and Trust Company Amended and Restated Short Term Incentive Plan (Incorporated by reference to Exhibit 10.35 of Form 10-Q Report for the quarter ended June 30, 2007, File No. 001-16691.)
10.26	*Onset Capital Corporation Employment Agreement. (Incorporated by reference to Exhibit 10.26 to Form 10-Q Report for the quarter ended June 30, 2002, File No. 000-06835.)
10.27	*Irwin Financial Corporation Restated Supplemental Executive Retirement Plan for Named Executives. (Incorporated by reference to Exhibit 10.27 to Form 10-Q Report for period ended June 30, 2002, File No. 000-06835.)
10.28	*Irwin Financial Corporation Supplemental Executive Retirement Plan for Named Executives. (Incorporated by reference to Exhibit 10.28 to Form 10-Q Report for the quarter ended June 30, 2002, File No. 000-06835.)
10.29	*Stock Purchase Agreement by and between Onset Holdings Inc. and Irwin International Corporation dated December 23, 2005. (Incorporated by reference to Exhibit 10.36 of Form 10-K Report for period ended December 31, 2005, File No. 001-16691.)
10.30	*Shareholder Agreement Termination Agreement by and between Irwin Commercial Finance Canada Corporation and Irwin International Corporation dated December 23, 2005. (Incorporated by reference to Exhibit 10.37 of Form 10-K Report for period ended December 31, 2005, File No. 001-16691.)
10.31	*Irwin Commercial Finance Corporation First Amended and Restated Shareholder Agreement dated May 15, 2007. (Incorporated by reference to Exhibit 10.41 of Form 10-Q Report for the quarter ended June 30, 2007, File No. 001-16691.)
10.32	*Irwin Commercial Finance Corporation 2005 Stock Option Agreement Grant of Option to Joseph LaLeggia dated December 23, 2005. (Incorporated by reference to Exhibit 10.39 of Form 10-K Report for period ended December 31, 2005, File No. 001-16691.)
10.33	*Irwin Commercial Finance Corporation 2005 Notice of Stock Option Grant to Joseph LaLeggia dated December 23, 2005. (Incorporated by reference to Exhibit 10.40 of Form 10-K Report for period ended December 31, 2005, File No. 001-16691.)
10.34	*Irwin Union Bank Amended and Restated Performance Unit Plan. (Incorporated by reference to Exhibit 10.41 of Form 10-K Report for period ended December 31, 2005, File No. 001-16691.)
10.35	*Irwin Commercial Finance Amended and Restated Performance Unit Plan. (Incorporated by reference to Exhibit 10.42 of Form 10-K Report for period ended December 31, 2005, File No. 001-16691.)
10.36	*First Amendment to the Irwin Commercial Finance Amended and Restated Performance Unit Plan, dated October 31, 2006. (Incorporated by reference to Exhibit 10.41 of Form 10-K report for the period ended December 31, 2006, File No. 001-16691.)

Edgar Filing: IRWIN FINANCIAL CORP - Form 10-K

- 10.37 *Irwin Home Equity Corporation Performance Unit Plan. (Incorporated by reference to Exhibit 10.43 of Form 10-K Report for period ended December 31, 2005, File No. 001-16691.)
- 10.38 *Supplemental Performance Unit Grant-Jocelyn Martin-Leano, dated February 6, 2007. (Incorporated by reference to Exhibit 10.45 of Form 10-K filed March 9, 2007, File No. 001-16691.)

Table of Contents

Exhibit Number	Description of Exhibit
10.39	*Irwin Financial Corporation 2007 Performance Unit Plan. (Incorporated by reference to Appendix B of the Corporation's 2007 Proxy Statement for the Annual Meeting of Shareholders, filed April 16, 2007, File No. 001-16691.)
10.40	Agreement General Release and Covenant Not to Sue between Irwin Financial Corporation, and Thomas D. Washburn executed December 5, 2007. (Incorporated by reference to Exhibit 99.1 of Form 8-K filed December 13, 2007, File No. 001-16691.)
11.1	Computation of Earnings Per Share.
12.1	Computation of Ratio of Earnings to Fixed Charges.
14.1	Code of Conduct.
21.1	Subsidiaries of Irwin Financial Corporation.
23.1	Consent of Independent Registered Public Accounting Firm.
23.2	Consent of Independent Registered Public Accounting Firm.
31.1	Certification pursuant to 18 U.S.C. Section 302 of the Sarbanes-Oxley Act of 2002 by the Chief Executive Officer.
31.2	Certification pursuant to 18 U.S.C. Section 302 of the Sarbanes-Oxley Act of 2002 by the Chief Financial Officer.
32.1	Certification of the Chief Executive Officer under Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of the Chief Financial Officer under Section 906 of the Sarbanes-Oxley Act of 2002.

* Indicates management contract or compensatory plan or arrangement

Table of Contents**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Corporation has duly caused this report to be signed on its behalf by the Undersigned, thereunto duly authorized.

IRWIN FINANCIAL CORPORATION

Date: March 12, 2008

By: /s/ William I. Miller
 William I. Miller
Chief Executive Officer, Chairman and President

Pursuant to the requirements of the Securities Exchange Act of 1934, this report on Form 10-K has been signed below by the following persons on behalf of the Corporation and in the capacities on the dates indicated.

Signature	Capacity with Corporation	Date
/s/ Sally A. Dean Sally A. Dean	Director	March 12, 2008
/s/ David W. Goodrich David W. Goodrich	Director	March 12, 2008
/s/ R. David Hoover R. David Hoover	Director	March 12, 2008
/s/ William H. Kling William H. Kling	Director	March 12, 2008
/s/ Brenda J. Lauderback Brenda J. Lauderback	Director	March 12, 2008
/s/ John C. McGinty, Jr. John C. McGinty, Jr.	Director	March 12, 2008
/s/ William I. Miller William I. Miller	Director, Chief Executive Officer, Chairman and President <i>(principal executive officer)</i>	March 12, 2008
/s/ Dayton H. Molendorp	Director	March 12, 2008

Dayton H. Molendorp

/s/ Lance R. Odden

Director

March 12, 2008

Lance R. Odden

/s/ Marita Zuraitis

Director

March 12, 2008

Marita Zuraitis

/s/ Gregory F. Ehlinger

Chief Financial Officer
(principal financial officer)

March 12, 2008

Gregory F. Ehlinger

/s/ Jody A. Littrell

First Vice President and Controller
(principal accounting officer)

March 12, 2008

Jody A. Littrell