

IMPAC MORTGAGE HOLDINGS INC

Form 10-Q

May 10, 2018

Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2018

or

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

For the transition period from to .

Commission File Number: 1-14100

IMPAC MORTGAGE HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

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

Maryland
(State or other jurisdiction of
incorporation or organization)

33-0675505
(I.R.S. Employer
Identification No.)

19500 Jamboree Road, Irvine, California 92612

(Address of principal executive offices)

(949) 475-3600

(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer

Accelerated filer

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

Smaller reporting
company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

There were 20,953,756 shares of common stock outstanding as of May 7, 2018.

Table of Contents

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

FORM 10-Q QUARTERLY REPORT

TABLE OF CONTENTS

| | Page |
|--|------|
| <u>PART I. FINANCIAL INFORMATION</u> | |
| <u>ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS</u> | |
| <u>Consolidated Balance Sheets as of March 31, 2018 (unaudited) and December 31, 2017</u> | 3 |
| <u>Consolidated Statements of Operations and Comprehensive Earnings for the Three Months Ended March 31, 2018 and 2017 (unaudited)</u> | 4 |
| <u>Consolidated Statement of Changes in Stockholders' Equity for the Three Months Ended March 31, 2018 (unaudited)</u> | 5 |
| <u>Consolidated Statements of Cash Flows for the Three Months Ended March 31, 2018 and 2017 (unaudited)</u> | 6 |
| <u>Notes to Unaudited Consolidated Financial Statements</u> | 7 |
| <u>ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u> | |
| <u>Forward-Looking Statements</u> | 28 |
| <u>The Mortgage Industry and Discussion of Relevant Fiscal Periods</u> | 28 |
| <u>Selected Financial Results</u> | 29 |
| <u>Status of Operations</u> | 29 |
| <u>Liquidity and Capital Resources</u> | 33 |
| <u>Critical Accounting Policies</u> | 34 |
| <u>Financial Condition and Results of Operations</u> | 35 |
| <u>ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u> | |
| <u>ITEM 4. CONTROLS AND PROCEDURES</u> | |
| <u>PART II. OTHER INFORMATION</u> | |
| <u>ITEM 1. LEGAL PROCEEDINGS</u> | |
| <u>ITEM 1A. RISK FACTORS</u> | |
| <u>ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS</u> | |
| <u>ITEM 3. DEFAULTS UPON SENIOR SECURITIES</u> | |
| <u>ITEM 4. MINE SAFETY DISCLOSURES</u> | |

| | |
|----------------------------------|----|
| <u>ITEM 5. OTHER INFORMATION</u> | 52 |
| <u>ITEM 6. EXHIBITS</u> | 53 |
| <u>SIGNATURES</u> | 54 |
| CERTIFICATIONS | |

Table of Contents

PART I. FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)

| | March 31, 2018 (Unaudited) | December 31, 2017 |
|---|----------------------------------|----------------------|
| ASSETS | | |
| Cash and cash equivalents | \$ 29,485 | \$ 33,223 |
| Restricted cash | 5,704 | 5,876 |
| Mortgage loans held-for-sale | 655,506 | 568,781 |
| Finance receivables | 26,989 | 41,777 |
| Mortgage servicing rights | 174,067 | 154,405 |
| Securitized mortgage trust assets | 3,524,053 | 3,670,550 |
| Goodwill | 104,587 | 104,587 |
| Intangible assets, net | 20,532 | 21,582 |
| Loans eligible for repurchase from Ginnie Mae | 54,632 | 47,697 |
| Other assets | 27,379 | 33,222 |
| Total assets | \$ 4,622,934 | \$ 4,681,700 |
| LIABILITIES | | |
| Warehouse borrowings | \$ 650,342 | \$ 575,363 |
| MSR financings | 45,000 | 35,133 |
| Convertible notes, net | 24,977 | 24,974 |
| Long-term debt | 45,337 | 44,982 |
| Securitized mortgage trust liabilities | 3,508,477 | 3,653,265 |
| Liability for loans eligible for repurchase from Ginnie Mae | 54,632 | 47,697 |
| Contingent consideration | — | 554 |
| Other liabilities | 33,970 | 34,585 |
| Total liabilities | 4,362,735 | 4,416,553 |

Commitments and contingencies (See Note 10)

STOCKHOLDERS' EQUITY

| | | |
|---|-----|-----|
| Series A-1 junior participating preferred stock, \$0.01 par value; 2,500,000 shares authorized; none issued or outstanding | — | — |
| Series B 9.375% redeemable preferred stock, \$0.01 par value; liquidation value \$16,640; 2,000,000 shares authorized, 665,592 noncumulative shares issued and outstanding as of March 31, 2018 and December 31, 2017 | 7 | 7 |
| Series C 9.125% redeemable preferred stock, \$0.01 par value; liquidation value \$35,127; 5,500,000 shares authorized; 1,405,086 noncumulative shares issued and outstanding as of March 31, 2018 and December 31, 2017 | 14 | 14 |
| Common stock, \$0.01 par value; 200,000,000 shares authorized; 20,952,679 and 20,949,679 shares issued and outstanding as of March 31, 2018 and | 210 | 209 |

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

| | | |
|--|--------------|--------------|
| December 31, 2017, respectively | | |
| Additional paid-in capital | 1,234,149 | 1,233,704 |
| Accumulated other comprehensive earnings, net of tax | 25,578 | — |
| Net accumulated deficit: | | |
| Cumulative dividends declared | (822,520) | (822,520) |
| Retained deficit | (177,239) | (146,267) |
| Net accumulated deficit | (999,759) | (968,787) |
| Total stockholders' equity | 260,199 | 265,147 |
| Total liabilities and stockholders' equity | \$ 4,622,934 | \$ 4,681,700 |

See accompanying notes to unaudited consolidated financial statements

Table of Contents

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE EARNINGS

(in thousands, except per share data)

(Unaudited)

| | For the Three Months Ended March 31, | |
|---|--|-----------|
| | 2018 | 2017 |
| Revenues: | | |
| Gain on sale of loans, net | \$ 21,482 | \$ 37,319 |
| Servicing fees, net | 9,463 | 7,320 |
| Gain (loss) on mortgage servicing rights, net | 7,705 | (977) |
| Real estate services fees, net | 1,385 | 1,633 |
| Other | 90 | 47 |
| Total revenues | 40,125 | 45,342 |
| Expenses: | | |
| Personnel expense | 17,742 | 24,919 |
| Business promotion | 9,731 | 10,231 |
| General, administrative and other | 8,275 | 8,023 |
| Accretion of contingent consideration | — | 845 |
| Change in fair value of contingent consideration | — | 539 |
| Total expenses | 35,748 | 44,557 |
| Operating income | 4,377 | 785 |
| Other income (expense): | | |
| Interest income | 50,150 | 61,584 |
| Interest expense | (49,130) | (61,138) |
| Change in fair value of long-term debt | 1,224 | (2,497) |
| Change in fair value of net trust assets, including trust REO gains | (2,138) | 6,319 |
| Total other income | 106 | 4,268 |
| Earnings before income taxes | 4,483 | 5,053 |
| Income tax expense | 610 | 426 |
| Net earnings | \$ 3,873 | \$ 4,627 |
| Other comprehensive earnings: | | |
| Change in fair value of instrument specific credit risk | \$ (1,440) | \$ — |
| Total comprehensive earnings | \$ 2,433 | \$ 4,627 |
| Earnings per common share: | | |
| Basic | \$ 0.18 | \$ 0.29 |
| Diluted | 0.18 | 0.29 |

See accompanying notes to unaudited consolidated financial statements

Table of Contents

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

(in thousands, except share amounts)

(Unaudited)

| | Preferred Shares Outstanding | Preferred Stock | Common Shares Outstanding | Common Stock | Additional Paid-In Capital | Cumulative Dividends Declared | Retained Deficit | Accumulated Other Comprehensive Earnings | Total Stock Equity |
|-------------------------|------------------------------------|--------------------|---------------------------------|-----------------|----------------------------------|-------------------------------------|---------------------|---|--------------------------|
| September 30, 2017 | 2,070,678 | \$ 21 | 20,949,679 | \$ 209 | \$ 1,233,704 | \$ (822,520) | \$ (146,267) | \$ — | \$ 260,000 |
| Issuance of stock | — | — | 3,000 | 1 | 15 | — | — | — | 16,000 |
| Share repurchase | — | — | — | — | 430 | — | — | — | 43,000 |
| Adoption of ASU 2016-01 | — | — | — | — | — | — | (27,018) | 27,018 | — |
| ASU related | — | — | — | — | — | — | (7,827) | — | (7,827) |
| Comprehensive | — | — | — | — | — | — | — | (1,440) | (1,440) |
| Dividends | — | — | — | — | — | — | 3,873 | — | 3,873 |
| September 30, 2018 | 2,070,678 | \$ 21 | 20,952,679 | \$ 210 | \$ 1,234,149 | \$ (822,520) | \$ (177,239) | \$ 25,578 | \$ 260,000 |

See accompanying notes to unaudited consolidated financial statements

Table of Contents

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(Unaudited)

| | For the Three Months Ended March 31, | |
|--|---|-------------|
| | 2018 | 2017 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net earnings | \$ 3,873 | \$ 4,627 |
| Loss on sale of mortgage servicing rights | — | 414 |
| Change in fair value of mortgage servicing rights | (9,180) | 1,122 |
| Gain on sale of mortgage loans | (28,851) | (31,595) |
| Change in fair value of mortgage loans held-for-sale | 4,891 | (5,203) |
| Change in fair value of derivatives lending, net | 1,815 | (79) |
| Provision (recovery) for repurchases | 378 | (1,666) |
| Origination of mortgage loans held-for-sale | (1,320,128) | (1,580,019) |
| Sale and principal reduction on mortgage loans held-for-sale | 1,246,881 | 1,558,851 |
| Gains from REO | (2,193) | (1,533) |
| Change in fair value of net trust assets, excluding REO | 4,331 | (4,786) |
| Change in fair value of long-term debt | (1,224) | 2,497 |
| Accretion of interest income and expense | 14,531 | 25,550 |
| Amortization of intangible and other assets | 1,193 | 1,192 |
| Accretion of contingent consideration | — | 845 |
| Change in fair value of contingent consideration | — | 539 |
| Amortization of debt issuance costs and discount on note payable | 21 | 100 |
| Stock-based compensation | 430 | 500 |
| Impairment of deferred charge | — | 276 |
| Excess tax benefit from share based compensation | — | 12 |
| Net change in other assets | (3,833) | 2,046 |
| Net change in other liabilities | (949) | (15,871) |
| Net cash used in operating activities | (88,014) | (42,181) |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Net change in securitized mortgage collateral | 116,205 | 182,824 |
| Proceeds from the sale of mortgage servicing rights | — | 481 |
| Finance receivable advances to customers | (165,668) | (183,613) |
| Repayments of finance receivables | 180,456 | 208,994 |
| Purchase of premises and equipment | (109) | (291) |
| Proceeds from the sale of REO | 5,418 | 6,859 |
| Net cash provided by investing activities | 136,302 | 215,254 |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Repayment of MSR financing | (25,133) | — |
| Borrowings under MSR financing | 35,000 | 35,133 |

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

| | | |
|---|-------------|-------------|
| Repayment of warehouse borrowings | (1,204,301) | (1,498,519) |
| Borrowings under warehouse agreements | 1,279,280 | 1,519,778 |
| Repayment of term financing | — | (30,000) |
| Payment of acquisition related contingent consideration | (554) | (7,958) |
| Repayment of securitized mortgage borrowings | (136,444) | (211,895) |
| Principal payments on capital lease | (59) | (101) |
| Debt issuance costs | — | (100) |
| Tax payments on stock based compensation awards | (3) | (21) |
| Proceeds from exercise of stock options | 16 | 30 |
| Net cash used in financing activities | (52,198) | (193,653) |
| Net change in cash, cash equivalents and restricted cash | (3,910) | (20,580) |
| Cash, cash equivalents and restricted cash at beginning of period | 39,099 | 46,067 |
| Cash, cash equivalents and restricted cash at end of period | \$ 35,189 | \$ 25,487 |
| NON-CASH TRANSACTIONS: | | |
| Transfer of securitized mortgage collateral to real estate owned | \$ 4,835 | \$ 2,267 |
| Mortgage servicing rights retained from loan sales and issuance of mortgage backed securities | 10,482 | 12,066 |

See accompanying notes to unaudited consolidated financial statements

Table of Contents

IMPAC MORTGAGE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

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

Note 1.—Summary of Business and Financial Statement Presentation

Business Summary

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

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

Financial Statement Presentation

The accompanying unaudited consolidated financial statements of IMH and its subsidiaries (as defined above) have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments, consisting of normal recurring adjustments considered necessary for a fair presentation, have been included. Operating results for the three months ended March 31, 2018 are not necessarily indicative of the results that may be expected for the year ending December 31, 2018. These interim period condensed consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements, which are included in the Company's Annual Report on Form 10-K for the year ended December 31, 2017, filed with the United States Securities and Exchange Commission (SEC).

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

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

Recent Accounting Pronouncements

Accounting Standards Update (ASU) No. 2014-09, 2015-04, 2016-08, 2016-10, 2016-12, 2016-20, 2017-13 and 2017-14, collectively implemented as Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC), "Revenue from Contracts with Customers (Topic 606)", provides guidance for revenue recognition.

This ASC's core principle requires a company to recognize revenue when it transfers promised goods or services to customers in an amount that reflects consideration to which the company expects to be entitled in exchange for those goods or services. The standard also clarifies the principal versus agent considerations, providing the evaluation must focus on whether the entity has control of the goods or services before they are transferred to the customer. The new standard permits the use of either the modified retrospective or full retrospective transition method. The Company's revenue is primarily generated from loan originations, loan servicing and real estate services. Origination revenue is comprised of fee income earned at origination of a loan, interest income earned for the period the loans are held and gain on sale on loans upon disposition of the loan. Servicing revenue is comprised of servicing fees and other ancillary fees in connection with our servicing activities. Real estate services revenue is comprised of income earned from various real estate services and support such as loss mitigation, loan modification, surveillance and disposition and monitoring services. The Company performed a

7

Table of Contents

review of the guidance as compared to current accounting policies and have evaluated all services rendered to customers as well as underlying contracts to determine the impact of this standard to the Company's revenue recognition process. The majority of services rendered by the Company in connection with loan originations, loan servicing and the long-term mortgage portfolio are not within the scope of FASB ASC 606. However, the Company identified real estate services revenues that were within the scope of FASB ASC 606 and the impact upon adoption was not materially different from the previous revenue recognition processes. The Company adopted this guidance on January 1, 2018, and the adoption of this ASU did not have a material impact on the Company's consolidated financial statements.

In January 2016, the FASB issued ASU 2016-01, "Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities." The amendments in ASU 2016-01, among other things, requires equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income; requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (i.e., securities or loans and receivables); requires separate presentation in other comprehensive income for the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments and eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost. The update is effective for interim and annual reporting periods beginning after December 15, 2017 on a modified retrospective basis, using a cumulative-effect adjustment to the balance sheet as of the beginning of the year adopted. The Company adopted this guidance on January 1, 2018, which resulted in a \$27.0 million reclass, net of tax, between opening retained earnings and other comprehensive income (loss) within stockholders' equity.

In August 2016, the FASB issued ASU 2016-15, "Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments." The update amends the guidance in Accounting Standards Codification 230, Statement of Cash Flows, and clarifies how entities should classify certain cash receipts and cash payments on the statement of cash flows with the objective of reducing the existing diversity in practice related to eight specific cash flow issues. In addition, in November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230), Restricted Cash (ASU 2016-18). This ASU clarifies certain existing principles in FASB ASC 230, including providing additional guidance related to transfers between cash and restricted cash and how entities present, in their statement of cash flows, the cash receipts and cash payments that directly affect the restricted cash accounts. These ASUs will be effective for the Company's fiscal year beginning after December 15, 2017 and subsequent interim periods. The Company adopted this guidance retrospectively on January 1, 2018. The adoption of this ASU did not have a material impact on the consolidated financial statements.

In October 2016, the FASB issued ASU 2016-16, "Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory." This ASU requires entities to recognize at the transaction date the income tax consequences of intercompany asset transfers other than inventory. This ASU is effective for public business entities for annual and interim periods in fiscal years beginning after December 15, 2017. The adoption of this standard was applied on a modified retrospective basis through a cumulative-effect adjustment directly to retained earnings as of the beginning

of the period of adoption. The Company adopted this guidance on January 1, 2018, which resulted in a \$7.8 million cumulative effect adjustment to opening retained earnings.

In May 2017, the FASB issued ASU 2017-09, "Compensation - Stock Compensation (Topic 718): Scope of Modification Accounting." The update provides guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. This ASU is effective for annual reporting periods beginning after December 15, 2017. The Company adopted this guidance on January 1, 2018, and the adoption of this ASU did not have a material impact on the Company's consolidated financial statements.

In February 2018, the FASB issued ASU 2018-02, "Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income." This ASU allows a reclassification from accumulated other comprehensive earnings (AOCE) to retained earnings for the stranded tax effects caused by the revaluation of deferred taxes resulting from the newly enacted corporate tax rate in the Tax Cuts and Jobs Act. The ASU is effective in years beginning after December 15, 2018, but permits early adoption in a period for which financial statements have not yet been issued. The Company does not expect the adoption of this ASU to have a material impact on its consolidated financial statements.

Table of Contents

In February 2018, the FASB ASU 2018-03, “Technical Corrections and Improvements to Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities.” This amendment clarifies certain aspects of the new guidance (ASU 2016-01) on recognizing and measuring financial instruments and presentation requirements for certain fair value option liabilities. ASU 2018-03 is effective for interim periods beginning after June 15, 2018 and will be effective for our 2018 annual reporting period. The standard requires entities to record a cumulative-effect adjustment to the statement of financial position at the beginning of the fiscal year in which the amendments are adopted. The Company does not expect the adoption of this ASU to have a material impact on its consolidated financial statements.

In March 2018, the FASB issued ASU 2018-05, “Income Taxes (Topic 740) - Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118.” This ASU codifies existing SEC guidance contained in SEC Staff Accounting Bulletin No. 118 (SAB 118), which expresses the view of the staff regarding application of existing guidance for the accounting for income taxes as it relates to the enactment of the Tax Cuts and Jobs Act (the TCJA) which was signed into law in the fourth quarter of 2017. In accordance with ASU 2018-05, the Company has recorded provisional estimates for the accounting impacts of the TCJA, deferred tax remeasurements, and other items, due to the uncertainty regarding how these provisions are to be implemented and additional anticipated forthcoming guidance. As management completes the analysis of the impacts of the TCJA, the Company may refine its current estimate and make adjustments, which will be recognized through income in the period such adjustments are identified, as required by ASU 2018-05.

Note 2.—Mortgage Loans Held-for-Sale

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

| | March 31, 2018 | December 31, 2017 |
|------------------------------------|-------------------|----------------------|
| Government (1) | \$ 179,150 | \$ 263,512 |
| Conventional (2) | 358,575 | 193,055 |
| Other (3) | 103,470 | 93,012 |
| Fair value adjustment (4) | 14,311 | 19,202 |
| Total mortgage loans held for sale | \$ 655,506 | \$ 568,781 |

-
- (1) Includes all government-insured loans including Federal Housing Administration (FHA), Veterans Affairs (VA) and United States Department of Agriculture (USDA).
 - (2) Includes loans eligible for sale to Federal National Mortgage Association (Fannie Mae or FNMA) and Federal Home Loan Mortgage Corporation (Freddie Mac or FHLMC).
 - (3) Includes non-qualified mortgages (NonQM) and jumbo loans.
 - (4) Changes in fair value are included in gain on sale of loans, net in the accompanying consolidated statements of operations.

Table of Contents

Gain on mortgage loans held-for-sale (LHFS), included in gain on sale of loans, net in the consolidated statements of operations, is comprised of the following the three months ended March 31, 2018 and 2017:

| | For the Three Months Ended March 31, | |
|---|--|-----------|
| | 2018 | 2017 |
| Gain on sale of mortgage loans | \$ 29,338 | \$ 38,240 |
| Premium from servicing retained loan sales | 10,482 | 12,066 |
| Unrealized losses from derivative financial instruments | (2,100) | (1,145) |
| Realized gains from derivative financial instruments | 12,045 | 1,125 |
| Mark to market (loss) gain on LHFS | (4,891) | 5,203 |
| Direct origination expenses, net | (23,014) | (19,836) |
| Provision for repurchases | (378) | 1,666 |
| Total gain on sale of loans, net | \$ 21,482 | \$ 37,319 |

Note 3.—Mortgage Servicing Rights

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

The following table summarizes the activity of MSRs for the three months ended March 31, 2018 and year ended December 31, 2017:

| March 31, 2018 | December 31, 2017 |
|-------------------|----------------------|
|-------------------|----------------------|

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

| | | |
|--|------------|------------|
| Balance at beginning of period | \$ 154,405 | \$ 131,537 |
| Additions from servicing retained loan sales | 10,482 | 56,049 |
| Addition from purchases | — | 5,618 |
| Reductions from bulk sales (1) | — | (895) |
| Changes in fair value (2) | 9,180 | (37,904) |
| Fair value of MSR's at end of period | \$ 174,067 | \$ 154,405 |

- (1) In the first quarter of 2017, the Company sold substantially all of its NonQM MSR's.
- (2) Changes in fair value are included within gain (loss) on MSR's, net in the accompanying consolidated statements of operations.

At March 31, 2018 and December 31, 2017, the outstanding principal balance of the mortgage servicing portfolio was comprised of the following:

| | March 31, 2018 | December 31, 2017 |
|----------------------|-------------------|----------------------|
| Government insured | \$ 3,346,717 | \$ 2,834,680 |
| Conventional (1) | 13,403,157 | 13,493,463 |
| NonQM | 1,947 | 1,957 |
| Total loans serviced | \$ 16,751,821 | \$ 16,330,100 |

- (1) At March 31, 2018 and December 31, 2017, \$13.4 billion and \$13.5 billion, respectively, of Fannie Mae and Freddie Mac servicing has been pledged as collateral as part of the MSR Financing (See Note 4.—Debt— MSR Financings). Pledged collateral

Table of Contents

was approximately 79% and 81% of the fair value of MSR's in the consolidated balance sheets at March 31, 2018 and December 31, 2017, respectively.

The table below illustrates hypothetical changes in fair values of MSR's, caused by assumed immediate changes to key assumptions that are used to determine fair value. See Note 6.—Fair Value of Financial Instruments for a description of the key assumptions used to determine the fair value of MSR's.

| | March 31, 2018 | December 31, 2017 |
|--|-------------------|----------------------|
| Mortgage Servicing Rights Sensitivity Analysis | | |
| Fair value of MSR's | \$ 174,067 | \$ 154,405 |
| Prepayment Speed: | | |
| Decrease in fair value from 10% adverse change | (4,418) | (5,643) |
| Decrease in fair value from 20% adverse change | (9,029) | (11,275) |
| Decrease in fair value from 30% adverse change | (13,752) | (16,807) |
| Discount Rate: | | |
| Decrease in fair value from 10% adverse change | (6,449) | (5,461) |
| Decrease in fair value from 20% adverse change | (12,449) | (10,555) |
| Decrease in fair value from 30% adverse change | (18,043) | (15,316) |

Sensitivities are hypothetical changes in fair value and cannot be extrapolated because the relationship of changes in assumptions to changes in fair value may not be linear. Also, the effect of a variation in a particular assumption is calculated without changing any other assumption, whereas a change in one factor may result in changes to another. Accordingly, no assurance can be given that actual results would be consistent with the results of these estimates. As a result, actual future changes in MSR values may differ significantly from those displayed above.

Gain (loss) on mortgage servicing rights, net is comprised of the following for the three months ended March 31, 2018 and 2017:

| | For the Three Months Ended March 31, | |
|---|--|------------|
| | 2018 | 2017 |
| Change in fair value of mortgage servicing rights | \$ 9,180 | \$ (1,122) |
| Loss on sale of mortgage servicing rights | (2) | (414) |
| Realized and unrealized (losses) gains from hedging instruments | (1,473) | 559 |
| Gain (loss) on mortgage servicing rights, net | \$ 7,705 | \$ (977) |

Servicing fees, net is comprised of the following for the three months ended March 31, 2018 and 2017:

| | For the Three Months Ended March 31, | |
|--|--|------|
| | 2018 | 2017 |

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

| | | |
|------------------------------|-----------|----------|
| Contractual servicing fees | \$ 11,538 | \$ 8,366 |
| Late and ancillary fees | 151 | 85 |
| Subservicing and other costs | (2,226) | (1,131) |
| Servicing fees, net | \$ 9,463 | \$ 7,320 |

Loans Eligible for Repurchase from Ginnie Mae (GNMA)

The Company routinely sells loans in GNMA guaranteed mortgage backed securities (MBS) by pooling eligible loans through a pool custodian and assigning rights to the loans to GNMA. When these GNMA loans are initially pooled and securitized, the Company meets the criteria for sale treatment and derecognizes the loans. The terms of the GNMA MBS program allow, but do not require, the Company to repurchase mortgage loans when the borrower has made no payments for three consecutive months. When the Company has the unconditional right, as servicer, to repurchase GNMA pool loans it has previously sold and are more than 90 days past due, the Company then re-recognizes the loans on its

Table of Contents

consolidated balance sheets in other assets, at their UPB, and records a corresponding liability in other liabilities in the consolidated balance sheets. At March 31, 2018 and December 31, 2017, loans eligible for repurchase from GNMA totaled \$54.6 million and \$47.7 million in UPB, respectively. As part of the Company's repurchase reserve, the Company records a repurchase provision to provide for estimated losses from the sale or securitization of all mortgage loans, including these loans.

The loans eligible for repurchase from GNMA are in the Company's servicing portfolio. The Company monitors the delinquency of the servicing portfolio and directs the servicer to mitigate losses on delinquent loans.

Note 4.—Debt

Warehouse Borrowings

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

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

| | Maximum Borrowing Capacity | Balance Outstanding At | | Maturity Date |
|----------------------------|----------------------------------|------------------------|----------------------|-------------------|
| | | March 31, 2018 | December 31, 2017 | |
| Short-term borrowings: | | | | |
| Repurchase agreement 1 | \$ 150,000 | \$ 127,272 | \$ 100,630 | June 15, 2018 |
| Repurchase agreement 2 | 35,000 | 31,172 | 31,632 | May 28, 2018 |
| Repurchase agreement 3 (1) | 225,000 | 150,345 | 154,020 | December 21, 2018 |
| Repurchase agreement 4 (2) | 250,000 | 131,745 | 152,772 | May 28, 2018 |
| Repurchase agreement 5 | 175,000 | 147,792 | 88,920 | January 31, 2019 |
| Repurchase agreement 6 | 200,000 | 61,848 | 47,389 | June 28, 2018 |
| Repurchase agreement 7 | 50,000 | 168 | — | December 26, 2018 |
| Total warehouse borrowings | \$ 1,085,000 | \$ 650,342 | \$ 575,363 | |

(1) As of March 31, 2018 and December 31, 2017, \$27.0 million and \$41.8 million, respectively, are associated with finance receivables made to the Company's warehouse customers.

(2) In April 2018, the maturity of the line was extended for 30 days to May 28, 2018, while the annual renewal is completed.

MSR Financings

On August 17, 2017, IMC (Borrower), entered into a Line of Credit Promissory Note with a lender providing for a revolving line of credit of \$30.0 million (FHLMC Financing). The Borrower is able to borrow up to 55% of the fair market value of FHLMC pledged mortgage servicing rights. The Line of Credit has a term until May 31, 2018 and will automatically renew for subsequent one year periods unless the lender provides the Borrowers 150 days' notice of its intention not to renew. Interest payments are payable monthly and accrue interest at the rate per annum equal to one-month LIBOR plus 4.0% and the balance of the obligation may be prepaid at any time. The obligations under the Line of Credit are secured by FHLMC pledged mortgage servicing rights and is guaranteed by Integrated Real Estate

Services, Corp. In February 2018, the maximum borrowing capacity of the revolving line of credit was increased to \$50.0 million and the term was extended to January 31, 2019. At March 31, 2018, \$30.0 million was outstanding under the FHLMC Financing and was secured by \$65.7 million of mortgage servicing rights.

On February 10, 2017, IMC (Borrower), entered into a Loan and Security Agreement (Agreement) with a lender providing for a revolving loan commitment of \$40.0 million for a period of two years (FNMA Financing). The Borrower is able to borrow up to 55% of the fair market value of FNMA pledged servicing rights. Upon the two year

Table of Contents

anniversary of the Agreement, any amounts outstanding will automatically be converted into a term loan due and payable in full on the one year anniversary of the conversion date. Interest payments are payable monthly and accrue interest at the rate per annum equal to one-month LIBOR plus 4.0% and the balance of the obligation may be prepaid at any time. The Borrower initially drew down \$35.1 million, and used a portion of the proceeds to pay off the Term Financing (approximately \$30.1 million) originally entered into in June 2015 as discussed below. The Borrower also paid the lender an origination fee of \$100 thousand, which is deferred and amortized over the life of the FNMA Financing. At March 31, 2018, \$15.0 million was outstanding under the FNMA Financing and was secured by \$71.4 million of mortgage servicing rights.

Convertible Notes

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

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

Unless an event of default has occurred and is continuing, each purchaser of the 2015 Convertible Notes agrees, for the three years after the Closing Date, to vote all Conversion Shares for each of the Company's nominees for election to the Company's board of directors and not to nominate any other candidate for election to the board of directors at any time within such three year period.

Long-term Debt

Junior Subordinated Notes

The Company carries its Junior Subordinated Notes at estimated fair value as more fully described in Note 6.—Fair Value of Financial Instruments. The following table shows the remaining principal balance and fair value of junior subordinated notes issued as of March 31, 2018 and December 31, 2017:

| | March 31, 2018 | December 31, 2017 |
|---------------------------------|-------------------|----------------------|
| Junior Subordinated Notes (1) | \$ 62,000 | \$ 62,000 |
| Fair value adjustment | (16,663) | (17,018) |
| Total Junior Subordinated Notes | \$ 45,337 | \$ 44,982 |

(1) Stated maturity of March 2034; requires quarterly distributions initially at a variable rate of 3 month LIBOR plus 3.75% per annum.

Table of Contents

Note 5.—Securitized Mortgage Trusts

Securitized Mortgage Trust Assets

Securitized mortgage trust assets, which are recorded at their estimated fair value (FMV), are comprised of the following at March 31, 2018 and December 31, 2017:

| | March 31, 2018 | December 31, 2017 |
|---|-------------------|----------------------|
| Securitized mortgage collateral | \$ 3,513,901 | \$ 3,662,008 |
| REO | 10,152 | 8,542 |
| Total securitized mortgage trust assets | \$ 3,524,053 | \$ 3,670,550 |

Securitized Mortgage Trust Liabilities

Securitized mortgage trust liabilities, which are recorded at their estimated FMV, are comprised of the following at March 31, 2018 and December 31, 2017:

| | March 31, 2018 | December 31, 2017 |
|---------------------------------|-------------------|----------------------|
| Securitized mortgage borrowings | \$ 3,508,477 | \$ 3,653,265 |

Changes in fair value of net trust assets, including trust REO losses, are comprised of the following for the three months ended March 31, 2018 and 2017:

| | For the Three Months Ended | |
|---|-------------------------------|----------|
| | March 31, 2018 | 2017 |
| Change in fair value of net trust assets, excluding REO | \$ (4,331) | \$ 4,786 |
| Gains from REO | 2,193 | 1,533 |
| Change in fair value of net trust assets, including trust REO gains | \$ (2,138) | \$ 6,319 |

Note 6.—Fair Value of Financial Instruments

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

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

Table of Contents

| | March 31, 2018 | | | | December 31, 2017 | | | |
|--------------------------------------|-----------------|------------------------------|------------------------------|-----------|-------------------|------------------------------|------------------------------|-----------|
| | Carrying Amount | Estimated Fair Value Level 1 | Estimated Fair Value Level 2 | Level 3 | Carrying Amount | Estimated Fair Value Level 1 | Estimated Fair Value Level 2 | Level 3 |
| Assets | | | | | | | | |
| Cash and cash equivalents | \$ 29,485 | \$ 29,485 | \$ — | \$ — | \$ 33,223 | \$ 33,223 | \$ — | \$ — |
| Restricted cash | 5,704 | 5,704 | — | — | 5,876 | 5,876 | — | — |
| Mortgage loans held-for-sale | 655,506 | — | 655,506 | — | 568,781 | — | 568,781 | — |
| Finance receivables | 26,989 | — | 26,989 | — | 41,777 | — | 41,777 | — |
| Mortgage servicing rights | 174,067 | — | — | 174,067 | 154,405 | — | — | 154,067 |
| Derivative assets, lending, net | 3,854 | — | — | 3,854 | 4,777 | — | 420 | 4,357 |
| Securitized mortgage collateral | 3,513,901 | — | — | 3,513,901 | 3,662,008 | — | — | 3,662,008 |
| Liabilities | | | | | | | | |
| Warehouse borrowings | \$ 650,342 | \$ — | \$ 650,342 | \$ — | \$ 575,363 | \$ — | \$ 575,363 | \$ — |
| MSR financings | 45,000 | — | — | 45,000 | 35,133 | — | — | 35,133 |
| Convertible notes | 24,977 | — | — | 24,977 | 24,974 | — | — | 24,974 |
| Contingent consideration | — | — | — | — | 554 | — | — | 554 |
| Long-term debt | 45,337 | — | — | 45,337 | 44,982 | — | — | 44,982 |
| Securitized mortgage borrowings | 3,508,477 | — | — | 3,508,477 | 3,653,265 | — | — | 3,653,265 |
| Derivative liabilities, lending, net | 892 | — | 892 | — | — | — | — | — |

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

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

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

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

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

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

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

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

MSR financings carrying amount approximates fair value as the underlying facility bears interest at a rate that is periodically adjusted based on a market index.

Table of Contents

Fair Value Hierarchy

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

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

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

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

As a result of the lack of observable market data resulting from inactive markets, the Company has classified its investment securities available-for-sale, mortgage servicing rights, securitized mortgage collateral and borrowings, derivative assets and liabilities (trust and IRLCs), and long-term debt as Level 3 fair value measurements. Level 3 assets and liabilities measured at fair value on a recurring basis were approximately 85% and 99% and 87% and 99%, respectively, of total assets and total liabilities measured at estimated fair value at March 31, 2018 and December 31, 2017.

Recurring Fair Value Measurements

The Company assesses the financial instruments on a quarterly basis to determine the appropriate classification within the fair value hierarchy, as defined by ASC Topic 810. Transfers between fair value classifications occur when there are changes in pricing observability levels. Transfers of financial instruments among the levels occur at the beginning of the reporting period. There were no material transfers between our Level 1 and Level 2 classified instruments during the three months ended March 31, 2018.

Table of Contents

The following tables present the Company's assets and liabilities that are measured at estimated fair value on a recurring basis, including financial instruments for which the Company has elected the fair value option at March 31, 2018 and December 31, 2017, based on the fair value hierarchy:

| | Recurring Fair Value Measurements | | | | | |
|--|-----------------------------------|-------------------|---------------------|-------------------|-------------------|---------------------|
| | March 31, 2018 | | | December 31, 2017 | | |
| | Level 1 | Level 2 | Level 3 | Level 1 | Level 2 | Level 3 |
| Assets | | | | | | |
| Mortgage loans held-for-sale | \$ — | \$ 655,506 | \$ — | \$ — | \$ 568,781 | \$ — |
| Derivative assets, lending, net (1) | — | — | 3,854 | — | 420 | 4,357 |
| Mortgage servicing rights | — | — | 174,067 | — | — | 154,405 |
| Securitized mortgage collateral | — | — | 3,513,901 | — | — | 3,662,008 |
| Total assets at fair value | \$ — | \$ 655,506 | \$ 3,691,822 | \$ — | \$ 569,201 | \$ 3,820,770 |
| Liabilities | | | | | | |
| Securitized mortgage borrowings | \$ — | \$ — | \$ 3,508,477 | \$ — | \$ — | \$ 3,653,265 |
| Long-term debt | — | — | 45,337 | — | — | 44,982 |
| Contingent consideration | — | — | — | — | — | 554 |
| Derivative liabilities, lending, net (2) | — | 892 | — | — | — | — |
| Total liabilities at fair value | \$ — | \$ 892 | \$ 3,553,814 | \$ — | \$ — | \$ 3,698,801 |

(1) At March 31, 2018, derivative assets, lending, net included \$3.9 million in IRLCs and is included in other assets in the accompanying consolidated balance sheets. At December 31, 2017, derivative assets, lending, net included \$4.4 million in IRLCs and \$420 thousand in Hedging instruments, respectively, and is included in other assets in the accompanying consolidated balance sheets.

(2) At March 31, 2018, derivative liabilities, lending, net included \$892 thousand in Hedging Instruments and is included in other liabilities in the accompanying consolidated balance sheets.

The following tables present reconciliations for all assets and liabilities measured at estimated fair value on a recurring basis using significant unobservable inputs (Level 3) for the three months ended March 31, 2018 and 2017:

| | Level 3 Recurring Fair Value Measurements For the Three Months Ended March 31, 2018 | | | | | |
|--|--|---------------------------------|---------------------------|-------------------------------------|----------------|--------------------------|
| | Securitized mortgage collateral | Securitized mortgage borrowings | Mortgage servicing rights | Interest rate lock commitments, net | Long-term debt | Contingent consideration |
| Fair value, December 31, 2017 | \$ 3,662,008 | \$ (3,653,265) | \$ 154,405 | \$ 4,357 | \$ (44,982) | \$ (554) |
| Total gains (losses) included in earnings: | | | | | | |
| Interest income (1) | 5,688 | — | — | — | — | — |
| Interest expense (1) | — | (20,080) | — | — | (139) | — |

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

| | | | | | | |
|--|--------------|----------------|------------|----------|-------------|------|
| Change in fair value | (32,755) | 28,424 | 9,180 | (503) | 1,224 | — |
| Change in instrument specific credit risk | — | — | — | — | (1,440) (2) | — |
| Total gains (losses) included in earnings | (27,067) | 8,344 | 9,180 | (503) | (355) | — |
| Transfers in and/or out of Level 3 | — | — | — | — | — | — |
| Purchases, issuances and settlements: | | | | | | |
| Purchases | — | — | — | — | — | — |
| Issuances | — | — | 10,482 | — | — | — |
| Settlements | (121,040) | 136,444 | — | — | — | 554 |
| Fair value, March 31, 2018 | \$ 3,513,901 | \$ (3,508,477) | \$ 174,067 | \$ 3,854 | \$ (45,337) | \$ — |
| Unrealized gains (losses) still held (3) | \$ (533,589) | \$ 2,694,742 | \$ 174,067 | \$ 3,854 | \$ 16,663 | \$ — |

(1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities. Net interest income, including cash received and paid, was \$2.2 million for three months ended March 31, 2018. The difference between accretion of interest income and expense and the amounts of interest income and expense recognized in the consolidated statements of operations is primarily from contractual interest on the securitized mortgage collateral and borrowings.

Table of Contents

- (2) Amount represents the change in instrument specific credit risk in other comprehensive earnings in the consolidated statements of operations and comprehensive earnings as required by the adoption of ASU 2016-01 on January 1, 2018.
- (3) Represents the amount of unrealized gains (losses) relating to assets and liabilities classified as Level 3 that are still held and reflected in the fair values at March 31, 2018.

Level 3 Recurring Fair Value Measurements
For the Three Months Ended March 31, 2017

| | Securitized mortgage collateral | Securitized mortgage borrowings | Mortgage servicing rights | Interest rate lock commitments, net | Long- term debt | Contingent consideration |
|--|---------------------------------------|---------------------------------------|---------------------------------|--|-----------------------|-----------------------------|
| Fair value, December 31, 2016 | \$ 4,021,891 | \$ (4,017,603) | \$ 131,537 | \$ 11,169 | \$ (47,207) | \$ (31,072) |
| Total gains (losses) included in earnings: | | | | | | |
| Interest income (1) | 15,484 | — | — | — | — | — |
| Interest expense (1) | — | (40,695) | — | — | (340) | — |
| Change in fair value | 51,052 | (46,266) | (1,122) | 1,164 | (2,497) | (1,384) |
| Total gains (losses) included in earnings | 66,536 | (86,961) | (1,122) | 1,164 | (2,837) | (1,384) |
| Transfers in and/or out of Level 3 | — | — | — | — | — | — |
| Purchases, issuances and settlements: | | | | | | |
| Purchases | — | — | — | — | — | — |
| Issuances | — | — | 12,066 | — | — | — |
| Settlements | (185,091) | 211,896 | (895) | — | — | 7,958 |
| Fair value, March 31, 2017 | \$ 3,903,336 | \$ (3,892,668) | \$ 141,586 | \$ 12,333 | \$ (50,044) | \$ (24,498) |
| Unrealized gains (losses) still held (2) | \$ (825,087) | \$ 2,977,521 | \$ 141,586 | \$ 12,333 | \$ 20,719 | \$ (24,498) |

- (1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities. Net interest income, including cash received and paid, was \$2.1 million for the three months ended March 31, 2017. The difference between accretion of interest income and expense and the amounts of interest income and expense recognized in the consolidated statements of operations is primarily from contractual interest on the securitized mortgage collateral and borrowings.
- (2) Represents the amount of unrealized gains (losses) relating to assets and liabilities classified as Level 3 that are still held and reflected in the fair values at March 31, 2017.

The following table presents quantitative information about the valuation techniques and unobservable inputs applied to Level 3 fair value measurements for financial instruments measured at fair value on a recurring and nonrecurring basis at March 31, 2018:

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

| Financial Instrument | Estimated Fair Value | Valuation Technique | Unobservable Input | Range of Inputs | Weighted Average |
|--|----------------------|---------------------|--------------------|-----------------|------------------|
| Assets and liabilities backed by real estate | | | | | |
| Securitized mortgage collateral, and | \$ 3,513,901 | DCF | Prepayment rates | 1.7 - 25.1 % | 7.1 % |
| Securitized mortgage borrowings | (3,508,477) | | Default rates | 0.01 - 4.2 % | 1.1 % |
| | | | Loss severities | 9.9 - 84.7 % | 46.1 % |
| | | | Discount rates | 3.9 - 25.0 % | 4.6 % |
| Other assets and liabilities | | | | | |
| Mortgage servicing rights | \$ 174,067 | DCF | Discount rate | 9.0 - 14.0 % | 9.7 % |
| | | | Prepayment rates | 6.9 - 88.8 % | 10.3 % |
| Derivative assets - IRLCs, net | 3,854 | Market pricing | Pull-through rate | 15.1 - 99.9 % | 78.5 % |
| Long-term debt | (45,337) | DCF | Discount rate | 9.9 % | 9.9 % |

DCF = Discounted Cash Flow

For assets and liabilities backed by real estate, a significant increase in discount rates, default rates or loss severities would result in a significantly lower estimated fair value. The effect of changes in prepayment speeds would have differing effects depending on the seniority or other characteristics of the instrument. For other assets and

Table of Contents

liabilities, a significant increase in discount rates would result in a significantly lower estimated fair value. A significant increase in one-month LIBOR would result in a significantly higher estimated fair value for derivative liabilities, net, securitized trusts. The Company believes that the imprecision of an estimate could be significant.

The following tables present the changes in recurring fair value measurements included in net earnings for the three months ended March 31, 2018 and 2017:

| Recurring Fair Value Measurements Changes in Fair Value Included in Net Earnings For the Three Months Ended March 31, 2018 | | | | | | | |
|--|-------------------------|--------------------|-------------------|---------------------|---------------------------|-------------------|--------------------|
| | Change in Fair Value of | | | | | | |
| | Interest | Interest | Net Trust | Long-term | Other | Gain on sale | |
| | Income (1) | Expense (1) | Assets | Debt | Revenue and Expense | of loans, net | Total |
| Securitized mortgage collateral | \$ 5,688 | \$ — | \$ (32,755) | \$ — | \$ — | \$ — | \$ (27,067) |
| Securitized mortgage borrowings | — | (20,080) | 28,424 | — | — | — | 8,344 |
| Derivative liabilities, net, securitized trusts | — | — | — | — | — | — | — |
| Long-term debt | — | (139) | — | 1,224 | — | — | 1,085 |
| Mortgage servicing rights (2) | — | — | — | — | 9,180 | — | 9,180 |
| Mortgage loans held-for-sale | — | — | — | — | — | (4,891) | (4,891) |
| Derivative assets — IRLCs | — | — | — | — | — | (503) | (503) |
| Derivative liabilities — Hedging Instruments | — | — | — | — | 285 | (1,597) | (1,312) |
| Total | \$ 5,688 | \$ (20,219) | \$ (4,331) | (3) \$ 1,224 | \$ 9,465 | \$ (6,991) | \$ (15,164) |

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

(2) Included in loss on MSRs, net in the consolidated statements of operations.

(3) For the three months ended March 31, 2018, change in the fair value of net trust assets, excluding REO was \$4.3 million.

| Recurring Fair Value Measurements Changes in Fair Value Included in Net Earnings For the Three Months Ended March 31, 2017 | | | | | | | |
|--|-------------------------|-------------|-----------|-----------|---------------------------|---------------|-------|
| | Change in Fair Value of | | | | | | |
| | Interest | Interest | Net Trust | Long-term | Other | Gain on sale | |
| | Income (1) | Expense (1) | Assets | Debt | Revenue and Expense | of loans, net | Total |

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

| | | | | | | | |
|---|-----------|-------------|-----------|----------------|------------|----------|-------------|
| Securitized mortgage collateral | \$ 15,484 | \$ — | \$ 51,052 | \$ — | \$ — | \$ — | \$ 66,536 |
| Securitized mortgage borrowings | — | (40,695) | (46,266) | — | — | — | (86,961) |
| Derivative liabilities, net, securitized trusts | — | — | — | — | — | — | — |
| Long-term debt | — | (340) | — | (2,497) | — | — | (2,837) |
| Mortgage servicing rights (2) | — | — | — | — | (1,122) | — | (1,122) |
| Contingent consideration | — | — | — | — | (1,384) | — | (1,384) |
| Mortgage loans held-for-sale | — | — | — | — | — | 5,203 | 5,203 |
| Derivative assets — IRLCs | — | — | — | — | — | 1,164 | 1,164 |
| Derivative liabilities — Hedging Instruments | — | — | — | — | 1,223 | (2,309) | (1,086) |
| Total | \$ 15,484 | \$ (41,035) | \$ 4,786 | (3) \$ (2,497) | \$ (1,283) | \$ 4,058 | \$ (20,487) |

- (1) Amounts primarily represent accretion to recognize interest income and interest expense using effective yields based on estimated fair values for trust assets and trust liabilities.
- (2) Included in loss on MSR, net in the consolidated statements of operations.
- (3) For the three months ended March 31, 2017, change in the fair value of net trust assets, excluding REO was \$4.8 million.

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

Mortgage servicing rights—The Company elected to carry its MSR arising from its mortgage loan origination operation at estimated fair value. The fair value of MSR is based upon market prices for similar instruments and a discounted cash flow model. The valuation model incorporates assumptions that market participants would use in

Table of Contents

estimating the fair value of servicing. These assumptions include estimates of prepayment speeds, discount rate, cost to service, escrow account earnings, contractual servicing fee income, prepayment and late fees, among other considerations. Mortgage servicing rights are considered a Level 3 measurement at March 31, 2018.

Mortgage loans held-for-sale—The Company elected to carry its mortgage loans held-for-sale originated or acquired at estimated fair value. Fair value is based on quoted market prices, where available, prices for other traded mortgage loans with similar characteristics, and purchase commitments and bid information received from market participants. Given the meaningful level of secondary market activity for mortgage loans, active pricing is available for similar assets and accordingly, the Company classifies its mortgage loans held-for-sale as a Level 2 measurement at March 31, 2018.

Securitized mortgage collateral—The Company elected to carry its securitized mortgage collateral at fair value. These assets consist primarily of non-conforming mortgage loans securitized between 2002 and 2007. Fair value measurements are based on the Company's internal models used to compute the net present value of future expected cash flows with observable market participant assumptions, where available. The Company's assumptions include its expectations of inputs that other market participants would use in pricing these assets. These assumptions include judgments about the underlying collateral, prepayment speeds, estimated future credit losses, forward interest rates, investor yield requirements and certain other factors. As of March 31, 2018, securitized mortgage collateral had UPB of \$4.0 billion, compared to an estimated fair value on the Company's balance sheet of \$3.5 billion. The aggregate UPB exceeds the fair value by \$0.5 billion at March 31, 2018. As of March 31, 2018, the UPB of loans 90 days or more past due was \$0.5 billion compared to an estimated fair value of \$0.2 billion. The aggregate UPB of loans 90 days or more past due exceed the fair value by \$0.3 billion at March 31, 2018. Securitized mortgage collateral is considered a Level 3 measurement at March 31, 2018.

Securitized mortgage borrowings—The Company elected to carry its securitized mortgage borrowings at fair value. These borrowings consist of individual tranches of bonds issued by securitization trusts and are primarily backed by non-conforming mortgage loans. Fair value measurements include the Company's judgments about the underlying collateral and assumptions such as prepayment speeds, estimated future credit losses, forward interest rates, investor yield requirements and certain other factors. As of March 31, 2018, securitized mortgage borrowings had an outstanding principal balance of \$4.0 billion, net of \$2.2 billion in bond losses, compared to an estimated fair value of \$3.5 billion. The aggregate outstanding principal balance exceeds the fair value by \$0.5 billion at March 31, 2018. Securitized mortgage borrowings are considered a Level 3 measurement at March 31, 2018.

Contingent consideration—Contingent consideration was applicable to the acquisition of CCM and was estimated and recorded at fair value at the acquisition date as part of purchase price consideration. Additionally, each reporting period, the Company estimated the change in fair value of the contingent consideration and any change in fair value is recognized in the Company's consolidated statements of operations if it is determined to not be a measurement period adjustment. The estimate of the fair value of contingent consideration required significant judgment and assumptions to be made about future operating results, discount rates and probabilities of various projected operating result scenarios. In the fourth quarter of 2017, the earn-out period ended and the remaining \$554 thousand in contingent consideration payments were paid during the three months ended March 31, 2018. Contingent consideration was considered a Level 3 measurement at March 31, 2017 and as of March 31, 2018, we have no further contingent consideration liability.

Long-term debt—The Company elected to carry its remaining long-term debt (consisting of junior subordinated notes) at fair value. These securities are measured based upon an analysis prepared by management, which considered the Company's own credit risk, including settlements with trust preferred debt holders and discounted cash flow analysis. As of March 31, 2018, long-term debt had UPB of \$62.0 million compared to an estimated fair value of \$45.3 million. The aggregate UPB exceeds the fair value by \$16.7 million at March 31, 2018. The long-term debt is considered a

Level 3 measurement at March 31, 2018.

Derivative assets and liabilities, Lending—The Company's derivative assets and liabilities are carried at fair value as required by GAAP and are accounted for as free standing derivatives. The derivatives include IRLCs with prospective residential mortgage borrowers whereby the interest rate on the loan is determined prior to funding and the

20

Table of Contents

borrowers have locked in that interest rate. These commitments are determined to be derivative instruments in accordance with GAAP. The derivatives also include hedging instruments (typically TBA MBS) used to hedge the fair value changes associated with changes in interest rates relating to its mortgage lending originations as well as mortgage servicing rights. The Company hedges the period from the interest rate lock (assuming a fall-out factor) to the date of the loan sale. The estimated fair value of IRLCs are based on underlying loan types with similar characteristics using the TBA MBS market, which is actively quoted and easily validated through external sources. The data inputs used in this valuation include, but are not limited to, loan type, underlying loan amount, note rate, loan program and expected sale date of the loan, adjusted for current market conditions. These valuations are adjusted at the loan level to consider the servicing release premium and loan pricing adjustments specific to each loan. For all IRLCs, the base value is then adjusted for the anticipated Pull-through Rate. The anticipated Pull-through Rate is an unobservable input based on historical experience, which results in classification of IRLCs as a Level 3 measurement at March 31, 2018.

The fair value of the Hedging Instruments is based on the actively quoted TBA MBS market using observable inputs related to characteristics of the underlying MBS stratified by product, coupon and settlement date. Therefore, the Hedging Instruments are classified as a Level 2 measurement at March 31, 2018.

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

| | Notional Amount | | Total Gains (Losses) (1) For the Three Months Ended | |
|----------------------|-------------------|----------------------|---|----------|
| | March 31, 2018 | December 31, 2017 | March 31, 2018 | 2017 |
| Derivative – IRLC's | \$ 354,117 | \$ 398,225 | \$ (503) | \$ 1,164 |
| Derivative – TBA MBS | 407,936 | 687,500 | 10,448 | (1,184) |

(1) Amounts included in gain on sale of loans, net within the accompanying consolidated statements of operations.
Nonrecurring Fair Value Measurements

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

The following tables present financial and non-financial assets and liabilities measured using nonrecurring fair value measurements at March 31, 2018 and 2017, respectively:

| | Nonrecurring Fair Value Measurements | | | | | |
|---------------------|--------------------------------------|----------|---------|----------------|----------|---------|
| | March 31, 2018 | | | March 31, 2017 | | |
| | Level 1 | Level 2 | Level 3 | Level 1 | Level 2 | Level 3 |
| REO (1) | \$ — | \$ 1,307 | \$ — | \$ — | \$ 6,342 | \$ — |
| Deferred charge (2) | — | — | — | — | — | 8,409 |

(1) Balance represents REO at March 31, 2018 which have been impaired subsequent to

foreclosure.

- (2) With the adoption of ASU 2016-16 on January 1, 2018, \$7.8 million in deferred charge was eliminated with a cumulative effect adjustment to opening retained earnings.

| | Total Gains (Losses) (1) For the Three Months Ended March 31, | |
|---------------------|---|----------|
| | 2018 | 2017 |
| REO (2) | \$ 2,193 | \$ 1,533 |
| Deferred charge (3) | — | (277) |

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

Table of Contents

- (2) For the three months ended March 31, 2018 and 2017, the Company recorded \$2.2 million and \$1.5 million, respectively, in gains which represent recovery of the net realizable value (NRV) attributable to an improvement in state specific loss severities on properties held during the period which resulted in an increase to NRV.
- (3) For the three months ended March 2017, the Company recorded \$277 thousand in income tax expense resulting from impairment write-downs of deferred charge based on changes in estimated cash flows and lives of the related mortgages retained in the securitized mortgage collateral. With the adoption of ASU 2016-16 on January 1, 2018, there will no longer be impairment of deferred charge.

Real estate owned—REO consists of residential real estate acquired in satisfaction of loans. Upon foreclosure, REO is adjusted to the estimated fair value of the residential real estate less estimated selling and holding costs, offset by expected contractual mortgage insurance proceeds to be received, if any. Subsequently, REO is recorded at the lower of carrying value or estimated fair value less costs to sell. REO balance representing REOs which have been impaired subsequent to foreclosure are subject to nonrecurring fair value measurement and included in the nonrecurring fair value measurements tables. Fair values of REO are generally based on observable market inputs, and considered Level 2 measurements at March 31, 2018.

Deferred charge—Deferred charge represented the deferral of income tax expense on inter-company profits that resulted from the sale of mortgages from taxable subsidiaries to IMH in prior years. The Company evaluated the deferred charge for impairment quarterly using internal estimates of estimated cash flows and lives of the related mortgages retained in the securitized mortgage collateral. If the deferred charge was determined to be impaired, it was recognized as a component of income tax expense. On January 1, 2018, the Company adopted ASU 2016-16, which resulted in a \$7.8 million cumulative effect adjustment to opening retained earnings eliminating the remaining deferred charge on the balance sheet. Deferred charge was considered a Level 3 measurement at March 31, 2017.

Note 7.—Income Taxes

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

The Company recorded income tax expense of \$610 thousand and \$426 thousand for the three months ended March 31, 2018 and 2017, respectively. Tax expense for the three months ended March 31, 2018 is primarily the result of state income taxes from states where the Company does not have net operating loss carryforwards or state minimum taxes, including AMT. Tax expense for the three months ended March 31, 2017 is primarily the result of amortization of the deferred charge and state income taxes from states where the Company does not have net operating loss carryforwards or state minimum taxes, including AMT.

The deferred charge represents the deferral of income tax expense on inter-company profits that resulted from the sale of mortgages from taxable subsidiaries to IMH prior to 2008. The deferred charge amortization and/or impairment, which does not result in any tax liability to be paid, is calculated based on the change in the estimated fair value of the underlying securitized mortgage collateral during the period. Prior to the adoption of ASU 2016-16 on January 1, 2018, the deferred charge was included in other assets in the accompanying consolidated balance sheets and was amortized as a component of income tax expense in the accompanying consolidated statements of operations.

As of December 31, 2017, the Company had estimated federal net operating loss (NOL) carryforwards of approximately \$619.9 million. Federal NOL carryforwards begin to expire in 2027. As of December 31, 2017, the Company had estimated California NOL carryforwards of approximately \$431.0 million, which begin to expire in 2028. The Company may not be able to realize the maximum benefit due to the nature and tax entities that holds the NOL.

Table of Contents

Note 8.—Reconciliation of Earnings Per Share

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

| | For the Three Months Ended March 31, | |
|--|--|----------|
| | 2018 | 2017 |
| Numerator for basic earnings per share: | | |
| Net earnings | \$ 3,873 | \$ 4,627 |
| Numerator for diluted earnings per share: | | |
| Net earnings | \$ 3,873 | \$ 4,627 |
| Interest expense attributable to convertible notes (1) | — | 454 |
| Net earnings plus interest expense attributable to convertible notes | \$ 3,873 | \$ 5,081 |
| Denominator for basic earnings per share (2): | | |
| Basic weighted average common shares outstanding during the period | 20,951 | 16,025 |
| Denominator for diluted earnings per share (2): | | |
| Basic weighted average common shares outstanding during the period | 20,951 | 16,025 |
| Net effect of dilutive convertible notes (1) | — | 1,163 |
| Net effect of dilutive stock options and DSU's | 151 | 234 |
| Diluted weighted average common shares | 21,102 | 17,422 |
| Net earnings per common share: | | |
| Basic | \$ 0.18 | \$ 0.29 |
| Diluted | \$ 0.18 | \$ 0.29 |

(1) Adjustments to diluted earnings per share for the convertible notes for the three months ended March 31, 2018 were excluded from the calculation as they are anti-dilutive.

(2) Number of shares presented in thousands.

At March 31, 2018, there were 1.2 million anti-dilutive stock options outstanding. There were 838 thousand anti-dilutive stock options outstanding the three months ended March 31, 2017.

Note 9.—Segment Reporting

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

Table of Contents

| Statement of Operations Items for the Three Months Ended March 31, 2018: | Mortgage Lending | Real Estate Services | Long-term Portfolio | Corporate and other | Consolidated |
|---|---------------------|----------------------------|------------------------|------------------------|--------------|
| Gain on sale of loans, net | \$ 21,482 | \$ — | \$ — | \$ — | \$ 21,482 |
| Real estate services fees, net | — | 1,385 | — | — | 1,385 |
| Servicing fees, net | 9,463 | — | — | — | 9,463 |
| Gain on mortgage servicing rights, net | 7,705 | — | — | — | 7,705 |
| Other revenue | — | — | 84 | 6 | 90 |
| Other operating expense | (31,548) | (638) | (65) | (3,497) | (35,748) |
| Other income (expense) | 334 | — | 196 | (424) | 106 |
| Net (loss) earnings before income tax expense | \$ 7,436 | \$ 747 | \$ 215 | \$ (3,915) | 4,483 |
| Income tax expense | | | | | 610 |
| Net earnings | | | | | \$ 3,873 |

| Statement of Operations Items for the Three Months Ended March 31, 2017: | Mortgage Lending | Real Estate Services | Long-term Portfolio | Corporate and other | Consolidated |
|---|---------------------|----------------------------|------------------------|------------------------|--------------|
| Gain on sale of loans, net | \$ 37,319 | \$ — | \$ — | \$ — | \$ 37,319 |
| Real estate services fees, net | — | 1,633 | — | — | 1,633 |
| Servicing fees, net | 7,320 | — | — | — | 7,320 |
| Loss on mortgage servicing rights, net | (977) | — | — | — | (977) |
| Other revenue | 14 | — | 61 | (28) | 47 |
| Accretion of contingent consideration | (845) | — | — | — | (845) |
| Change in fair value of contingent consideration | (539) | — | — | — | (539) |
| Other operating expense | (38,085) | (995) | (86) | (4,007) | (43,173) |
| Other income (expense) | 407 | — | 4,713 | (852) | 4,268 |
| Net (loss) earnings before income tax expense | \$ 4,614 | \$ 638 | \$ 4,688 | \$ (4,887) | \$ 5,053 |
| Income tax expense | | | | | 426 |
| Net earnings | | | | | \$ 4,627 |

| Balance Sheet Items as of: | Mortgage Lending | Real Estate Services | Long-term Portfolio | Corporate and other | Consolidated |
|---------------------------------------|---------------------|----------------------------|------------------------|------------------------|--------------|
| Total Assets at March 31, 2018 (1) | \$ 1,089,230 | \$ — | \$ 3,523,949 | \$ 9,755 | \$ 4,622,934 |
| Total Assets at December 31, 2017 (1) | \$ 992,983 | \$ 251 | \$ 3,678,377 | \$ 10,089 | \$ 4,681,700 |

(1) All segment asset balances exclude intercompany balances.

Note 10.—Commitments and Contingencies

Legal Proceedings

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

In accordance with applicable accounting guidance, the Company establishes an accrued liability for litigation when those matters present loss contingencies that are both probable and estimable. In any case, there may be an exposure to losses in excess of any such amounts whether accrued or not. Any estimated loss is subject to significant judgment and is based upon currently available information, a variety of assumptions, and known and unknown

Table of Contents

uncertainties. The matters underlying the estimated loss will change from time to time, and actual results may vary significantly from the current estimate. Therefore, an estimate of possible loss represents what the Company believes to be an estimate of possible loss only for certain matters meeting these criteria. It does not represent the Company's maximum loss exposure.

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

The legal matter updates summarized below are ongoing and may have an effect on the Company's business and future financial condition and results of operations:

On April 30, 2012, a purported class action was filed entitled *Marentes v. Impac Mortgage Holdings, Inc.*, alleging that certain loan modification activities of the Company constitute an unfair business practice, false advertising and marketing, and that the fees charged are improper. The complaint seeks unspecified damages, restitution, injunctive relief, attorney's fees and prejudgment interest. On August 22, 2012, the plaintiff filed an amended complaint adding Impac Funding Corporation as a defendant and on October 2, 2012, the plaintiff dismissed Impac Mortgage Holdings, Inc., without prejudice. Trial is currently scheduled for June 2018.

On November 1, 2016, a qui tam action was filed under seal entitled *United States of America ex rel Jeremy Calva, et al. v. Impac Secured Assets Corp., et al.* The matter was unsealed on November 3, 2017. The complaint alleges the defendants violated the False Claims Act by misrepresenting loan delinquency rates for loans deposited into certain securitization trusts, not notifying the trustee of certain trusts that delinquent loans were deposited into the trusts, not notifying anyone that Company affiliates were the originator of most loans as well as the sponsor, depositor, issuer, and master servicer of certain trusts, causing government entities to buy bonds in those trusts. The complaint seeks an order that the defendants cease and desist from submitting false claims to the plaintiffs, as well as civil penalties, damages, attorneys' fees, and costs incurred in the case. Neither the United States, nor any of the states or cities named as plaintiff in the matter elected to intervene in the case. The defendants filed a motion to dismiss the complaint on March 23, 2018.

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

Please refer to IMH's report on Form 10-K for the year ended December 31, 2017 for a description of litigation and claims.

Repurchase Reserve

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

The following table summarizes the repurchase reserve activity, within other liabilities on the consolidated balance sheets, related to previously sold loans for the three months ended March 31, 2018 and year ended December 31, 2017:

25

Table of Contents

| | March 31, 2018 | December 31, 2017 |
|---------------------------|-------------------|----------------------|
| Beginning balance | \$ 6,020 | \$ 5,408 |
| Provision for repurchases | 378 | 1,557 |
| Settlements | (946) | (945) |
| Total repurchase reserve | \$ 5,452 | \$ 6,020 |

Short-Term Loan Commitments

The Company uses a portion of its warehouse borrowing capacity to provide secured short-term revolving financing to small and medium-size mortgage originators to finance mortgage loans from the closing of the mortgage loans until sold to investors (Finance Receivables). As of March 31, 2018, the warehouse lending operations had warehouse lines to non-affiliated customers totaling \$122.5 million, of which there was an outstanding balance of \$27.0 million in finance receivables compared to \$41.8 million as of December 31, 2017. The finance receivables are generally secured by residential mortgage loans as well as personal guarantees.

Commitments to Extend Credit

The Company enters into IRLCs with prospective borrowers whereby the Company commits to lend a certain loan amount under specific terms and interest rates to the borrower. These loan commitments are treated as derivatives and are carried at fair value. See Note 6. — Fair Value of Financial Instruments for more information.

Note 11.—Equity and Share Based Payments

The following table summarizes activity, pricing and other information for the Company's stock options for the three months ended March 31, 2018:

| | Number of Shares | Weighted- Average Exercise Price |
|--|---------------------|---|
| Options outstanding at December 31, 2017 | 1,582,754 | \$ 13.61 |
| Options granted | — | — |
| Options exercised | (3,000) | 5.39 |
| Options forfeited/cancelled | (72,623) | 16.31 |
| Options outstanding at March 31, 2018 | 1,507,131 | 13.50 |
| Options exercisable at March 31, 2018 | 917,801 | \$ 12.04 |

As of March 31, 2018, there was approximately \$2.5 million of total unrecognized compensation cost related to stock option compensation arrangements granted under the plan, net of estimated forfeitures. That cost is expected to be recognized over the remaining weighted average period of 1.8 years.

Table of Contents

The following table summarizes activity, pricing and other information for the Company's DSU's, also referred to as deferred stock units as the issuance of the stock is deferred until termination of service, for the three months ended March 31, 2018:

| | Number of Shares | Weighted- Average Grant Date Fair Value |
|--|---------------------|--|
| DSU's outstanding at December 31, 2017 | 100,750 | \$ 10.41 |
| DSU's granted | — | — |
| DSU's exercised | — | — |
| DSU's forfeited/cancelled | — | — |
| DSU's outstanding at March 31, 2018 | 100,750 | \$ 10.41 |

As of March 31, 2018, there was approximately \$203 thousand of total unrecognized compensation cost related to the DSU compensation arrangements granted under the plan. That cost is expected to be recognized over a weighted average period of 2.2 years.

Note 12.—Subsequent Events

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

Table of Contents

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

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

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

Forward-Looking Statements

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

For a discussion of these and other risks and uncertainties that could cause actual results to differ from those contained in the forward-looking statements, see "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Company's Annual Report on Form 10-K for the period ended December 31, 2017, and other reports we file under the Securities Exchange Act of 1934. This document speaks only as of its date and we do not undertake, and specifically disclaim any obligation, to release publicly the results of any revisions that may be made to any forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date of such statements.

The Mortgage Industry and Discussion of Relevant Fiscal Periods

The mortgage industry is subject to current events that occur in the financial services industry including changes to regulations and compliance requirements that result in uncertainty surrounding the actions of states, municipalities and government agencies, including the Consumer Financial Protection Bureau (CFPB) and Federal Housing Finance

Agency (FHFA). These events can also include changes in economic indicators, interest rates, price competition, geographic shifts, disposable income, housing prices, market liquidity, market anticipation, environmental conditions, such as hurricanes and floods, and customer perception, as well as others. The factors that affect the industry change rapidly and can be unforeseeable making it difficult to predict and manage an operation in the financial services industry.

Table of Contents

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

Selected Financial Results

| | For the Three Months Ended | | |
|---|----------------------------|----------------------|-------------------|
| | March 31, 2018 | December 31, 2017 | March 31, 2017 |
| Revenues: | | | |
| Gain on sale of loans, net | \$ 21,482 | \$ 19,545 | \$ 37,319 |
| Servicing fees, net | 9,463 | 8,327 | 7,320 |
| Gain (loss) on mortgage servicing rights, net | 7,705 | (17,721) | (977) |
| Real estate services fees, net | 1,385 | 1,364 | 1,633 |
| Other | 90 | 140 | 47 |
| Total revenues | 40,125 | 11,655 | 45,342 |
| Expenses: | | | |
| Personnel expense | 17,742 | 20,294 | 24,919 |
| Business promotion | 9,731 | 9,532 | 10,231 |
| General, administrative and other | 8,275 | 12,931 | 8,023 |
| Accretion of contingent consideration | — | 109 | 845 |
| Change in fair value of contingent consideration | — | (2,273) | 539 |
| Total expenses | 35,748 | 40,593 | 44,557 |
| Operating income (loss): | 4,377 | (28,938) | 785 |
| Other income (expense): | | | |
| Net interest income | 1,020 | 1,253 | 446 |
| Change in fair value of long-term debt | 1,224 | (292) | (2,497) |
| Change in fair value of net trust assets | (2,138) | (365) | 6,319 |
| Total other income | 106 | 596 | 4,268 |
| Net earnings (loss) before income taxes | 4,483 | (28,342) | 5,053 |
| Income tax expense | 610 | 16,563 | 426 |
| Net earnings (loss) | \$ 3,873 | \$ (44,905) | \$ 4,627 |
| Other comprehensive earnings: | | | |
| Change in fair value of instrument specific credit risk | (1,440) | — | — |
| Total comprehensive earnings | \$ 2,433 | \$ (44,905) | \$ 4,627 |
| | | | |
| Diluted weighted average common shares | 21,102 | 20,949 | 17,422 |
| Diluted earnings per share | \$ 0.18 | \$ (2.14) | \$ 0.29 |

Status of Operations

Summary Highlights

- Mortgage servicing portfolio increased to \$16.8 billion at March 31, 2018 from \$16.3 billion at December 31, 2017 and \$13.2 billion at March 31, 2017.

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

- Servicing fees, net increased to \$9.5 million for the three months ended March 31, 2018 from \$8.3 million for the three months ended December 31, 2017 and \$7.3 million for the three months ended March 31, 2017.
- NonQM mortgage origination volumes increased to \$248.2 million in the first quarter of 2018 from \$235.0 million in the fourth quarter of 2017 and \$184.3 million in the first quarter of 2017.
- Mortgage servicing rights (MSRs) increased to \$174.1 million at March 31, 2018 as compared to \$154.4 million at December 31, 2017 and \$141.6 million at March 31, 2017.

For the first quarter of 2018, we reported net earnings of \$3.9 million, or \$0.18 per diluted common share, as compared to net earnings of \$4.6 million, or \$0.29 per diluted common share, for the first quarter of 2017. For the first

Table of Contents

quarter of 2018, adjusted operating income (loss) (as defined below) was \$4.4 million, or \$0.21 per diluted common share, as compared to \$2.2 million, or \$0.12 per diluted common share, for the first quarter of 2017.

Net earnings primarily decreased due to a decline in gain on sale of loans revenue as a result of a decrease in origination volumes as well as a decline in margins. Gain on sale margins decreased by 73 basis point (bps) to 163 bps in the first quarter of 2018, as compared to 236 bps in the first quarter of 2017 reflecting the margin compression resulting from the historically low interest rate environment, in which the Company was able to generate significantly larger volume with wide gain on sale margins. Despite the decline in net earnings as compared to the first quarter of 2017, adjusted operating income (loss) increased as a result of the change in estimated fair value of MSRs and a decline in operating expenses.

Operating income (loss), excluding the changes in contingent consideration (adjusted operating income (loss)), which is not considered an accounting principle generally accepted in the United States of America (non-GAAP) financial measurement; see the discussion and reconciliation on non-GAAP financial measures below.

Net earnings (loss) include fair value adjustments for changes in the contingent consideration (which ended in December 2017), long-term debt and net trust assets. The contingent consideration is related to the CashCall Mortgage (CCM) acquisition transaction, while the other fair value adjustments are related to our legacy portfolio. These fair value adjustments are non-cash items and are not related to current operating results. Although we are required to record change in fair value and accretion of the contingent consideration, management believes operating income excluding contingent consideration changes and the related accretion is more useful to discuss our ongoing and future operations.

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

| | For the Three Months Ended | | |
|---------------------------------------|----------------------------|----------------------|-------------------|
| | March 31, 2018 | December 31, 2017 | March 31, 2017 |
| Net earnings (loss): | \$ 3,873 | \$ (44,905) | \$ 4,627 |
| Total other (income) expense | (106) | (596) | (4,268) |
| Income tax expense | 610 | 16,563 | 426 |
| Operating income (loss): | \$ 4,377 | \$ (28,938) | \$ 785 |
| Accretion of contingent consideration | — | 109 | 845 |

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

| | | | |
|--|----------|-------------|----------|
| Change in fair value of contingent consideration | — | (2,273) | 539 |
| Adjusted operating income (loss) | \$ 4,377 | \$ (31,102) | \$ 2,169 |
| Diluted weighted average common shares | 21,102 | 20,949 | 17,422 |
| Diluted adjusted operating income (loss) per share | \$ 0.21 | \$ (1.48) | \$ 0.12 |
| Diluted earnings (loss) per share | \$ 0.18 | \$ (2.14) | \$ 0.29 |
| Adjustments: | | | |
| Total other (income) expense (1) | (0.01) | (0.03) | (0.27) |
| Income tax expense | 0.04 | 0.79 | 0.02 |
| Accretion of contingent consideration | — | 0.01 | 0.05 |
| Change in fair value of contingent consideration | — | (0.11) | 0.03 |
| Diluted adjusted operating income (loss) per share | \$ 0.21 | \$ (1.48) | \$ 0.12 |

Table of Contents

- (1) Except for when anti-dilutive, convertible debt interest expense, net of tax, is included for calculating diluted earnings per share (EPS) and is excluded for purposes of reconciling GAAP diluted EPS to non-GAAP diluted adjusted operating income (loss) per share.

Originations

| (in millions) | For the Three Months Ended | | | March 31, 2017 | % | March 31, 2017 | % |
|--------------------|----------------------------|----------------------|-------------|-------------------|--------|-------------------|---|
| | March 31, 2018 | December 31, 2017 | % Change | | | | |
| Retail | \$ 631.1 | \$ 932.3 | (32) % | \$ 1,066.2 | (41) % | | |
| Correspondent | 479.6 | 467.0 | 3 | 271.2 | 77 | | |
| Wholesale | 209.4 | 254.5 | (18) | 242.6 | (14) | | |
| Total originations | \$ 1,320.1 | \$ 1,653.8 | (20) | \$ 1,580.0 | (16) | | |

During the first quarter of 2018, total originations decreased 20% to \$1.3 billion as compared to \$1.7 billion in the fourth quarter of 2017 and decreased 16% as compared to \$1.6 billion in the first quarter of 2017. The decrease in originations from the fourth and first quarters of 2017 was a result of higher interest rates. From January 2017 through the first quarter of 2018, interest rates have increased 100 bps from the historically low interest rate environment the previous years, causing a sharp drop in refinance volume.

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

Originations by Loan Type:

| (in millions) | For the Three Months Ended March 31, | |
|--------------------|---|------------|
| | 2018 | 2017 |
| Conventional | \$ 520.1 | \$ 967.3 |
| Government (1) | 551.8 | 428.4 |
| NonQM | 248.2 | 184.3 |
| Total originations | \$ 1,320.1 | \$ 1,580.0 |

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

During the first quarter of 2018, the origination volume of NonQM loans increased to \$248.2 million, as compared to \$235.0 million in the fourth quarter of 2017 and \$184.3 million in the first quarter of 2017. In the first quarter of 2018, the retail channel accounted for 23% of NonQM originations while the wholesale and correspondent channels accounted for 77% of NonQM production. In the fourth quarter of 2017, the retail channel accounted for just 27% of

NonQM originations, while the wholesale and correspondent channels accounted for 73% of NonQM production. The NonQM loans originated since 2016 have all been sold on a servicing released basis.

We continue to believe there is an underserved mortgage market for borrowers with good credit who may not meet the qualified mortgage (QM) guidelines set out by the Consumer Financial Protection Bureau (CFPB). NonQM borrowers generally have a good credit history but income documentation that does not allow them to qualify for an agency loan, such as a self-employed borrower. We have established strict lending guidelines, including determining the prospective borrowers' ability to repay the mortgage, which we believe will keep delinquencies and foreclosures at acceptable levels. We continue to refine our guidelines to expand our reach to the underserved market of credit worthy borrowers who can fully document and substantiate an ability to repay mortgage loans, but unable to obtain financing through traditional programs (QM loans), for example self-employed borrowers.

Table of Contents

We have established investor relationships for these products that provide us with an exit strategy for these nonconforming loans. In the first quarter of 2018, our NonQM origination volume was \$248.2 million with an average FICO of 720 and a weighted average LTV of 66%.

Originations by Purpose:

| (in millions) | For the Three Months Ended March 31, | | | |
|--------------------|--------------------------------------|------|------------|------|
| | 2018 | % | 2017 | % |
| Refinance | \$ 878.4 | 67 % | \$ 1,244.4 | 79 % |
| Purchase | 441.7 | 33 | 335.6 | 21 |
| Total originations | \$ 1,320.1 | 100 | \$ 1,580.0 | 100 |

During the first quarter of 2018, refinance volume decreased approximately 29% to \$878.4 million as compared to \$1.2 billion in the first quarter of 2017 as a result of rising interest rates throughout 2017 and continuing in the first quarter of 2018. Despite the 16% decrease in origination volumes during the first quarter of 2018, purchase money transactions increased 32% to \$441.7 million as compared to \$335.6 million in the first quarter of 2017.

Mortgage servicing portfolio

| (in millions) | March 31, | December 31, | % | March 31, | % |
|------------------------------|-------------|--------------|--------|-------------|--------|
| | 2018 | 2017 | Change | 2017 | Change |
| Mortgage servicing portfolio | \$ 16,751.8 | \$ 16,330.1 | 3 % | \$ 13,241.9 | 27 % |

The mortgage servicing portfolio increased to \$16.8 billion at March 31, 2018 as compared to \$16.3 billion at December 31, 2017 and \$13.2 billion at March 31, 2017. During 2018, we have continued with our strategy of growing the mortgage servicing portfolio. During the three months ended March 31, 2018, the mortgage servicing portfolio increased due to servicing retained loan sales of \$974.7 million in unpaid principal balance (UPB). As a result, the UPB of our mortgage servicing portfolio increased 27% to \$16.8 billion as of March 31, 2018 from March 31, 2017. The servicing portfolio generated net servicing income of \$9.5 million in the first quarter of 2018, a 29% increase over the net servicing fees of \$7.3 million in the first quarter of 2017. Delinquencies within the servicing portfolio have decreased slightly and remain low at 0.72% for 60+ days delinquent as of March 31, 2018 as compared to 0.81% as of December 31, 2017. With the acquisition of MSRs in the second quarter of 2017, we added Specialized Loan Servicing LLC as a subservicer in addition to our current subservicer LoanCare, LLC.

The following table includes information about our mortgage servicing portfolio:

| (in millions) | At March 31, | % 60+ days | At December 31, | % 60+ days |
|---------------|--------------|----------------|-----------------|----------------|
| | 2018 | delinquent (1) | 2017 | delinquent (1) |
| Fannie Mae | \$ 7,269.2 | 0.21 % | \$ 7,518.2 | 0.32 % |
| Freddie Mac | 6,133.9 | 0.22 | 5,975.3 | 0.29 |

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

| | | | | |
|---------------------------|-------------|-------|-------------|-------|
| Ginnie Mae | 3,346.7 | 2.48 | 2,834.7 | 2.90 |
| Other | 2.0 | 16.67 | 1.9 | 16.67 |
| Total servicing portfolio | \$ 16,751.8 | 0.72 | \$ 16,330.1 | 0.81 |

(1) Based on loan count.

During the three months ended March 31, 2018, our warehouse borrowing capacity increased from \$960.0 million to \$1.1 billion. In addition to funding our mortgage loan originations, we also used a portion of our warehouse borrowing capacity to provide re warehouse facilities to our customers, correspondent sellers and other small mortgage banking companies represented as finance receivables on the consolidated balance sheets. The outstanding balance of finance receivables decreased to \$27.0 million at March 31, 2018 as compared to \$41.8 million at December 31, 2017. The warehouse lending division funding volumes decreased to \$165.7 million during the first quarter of 2018 as compared to \$183.6 million for the first quarter of 2017. By leveraging our re warehousing division, our strategy is to increase the capture rate of our approved correspondent sellers business as well as expand our active customer base to include new customers seeking warehouse lines.

32

Table of Contents

For the first quarter of 2018, real estate services fees were \$1.4 million as compared to \$1.4 million in the fourth quarter of 2017 and \$1.6 million in the first quarter of 2017. Most of our real estate services business is generated from our long-term mortgage portfolio, as the long term mortgage portfolio continues to decline, we expect real estate services and the related revenues to decline.

In our long-term mortgage portfolio, the residual interests generated cash flows of \$1.8 million in the first quarter of 2018 as compared to \$1.7 million in the fourth quarter of 2017 and \$5.1 million in the first quarter of 2017. The estimated fair value of the net residual interests decreased \$1.7 million in the first quarter of 2018 to \$15.6 million at March 31, 2018, as a result of an increase in forward LIBOR as well as residual cash flows received partially offset by an improvement in performance from certain trusts.

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

Liquidity and Capital Resources

During the three months ended March 31, 2018, we funded our operations primarily from mortgage lending revenues and to a lesser extent real estate services fees and cash flows from our residual interests in securitizations. Mortgage lending revenues include gains on sale of loans, net, and other mortgage related income, and real estate services fees including portfolio loss mitigation fees primarily generated from our long-term mortgage portfolio. Additionally, we funded mortgage loan originations using warehouse facilities which are repaid once the loan is sold. We may continue to manage our capital through the financing or sale of mortgage servicing rights. We may also seek to raise capital by issuing debt or equity, including offering shares through the “At-the-Market” offering (ATM) program we initiated in 2015.

On August 17, 2017, IMC (Borrower), issued a Line of Credit Promissory Note with a lender providing for a revolving line of credit of \$30.0 million (Freddie Mac Financing). The Borrower is able to borrow up to 55% of the fair market value of Freddie Mac pledged mortgage servicing rights. In February 2018, the maximum borrowing capacity of the revolving line of credit was increased to \$50.0 million and the term was extended to January 31, 2019.

Interest payments are payable monthly and accrue interest at the rate per annum equal to LIBOR plus 4.0% and the balance of the obligation may be prepaid at any time. The obligations under the Freddie Mac Financing are secured by Freddie Mac pledged mortgage servicing rights and Integrated Real Estate Services, Corp. is a guarantor. At March 31, 2018, \$30.0 million was outstanding under the Freddie Mac Financing and was secured by \$65.7 million of mortgage servicing rights.

In February 2017, we entered into a Loan and Security Agreement (Agreement) with a lender providing for a revolving loan commitment of up to \$40.0 million for a period of two years (Fannie Mae Financing) to finance MSR. We are able to borrow up to 55% of the fair market value of Fannie Mae pledged servicing rights. Upon the two year anniversary of the Agreement, any amounts outstanding will automatically be converted into a term loan due and payable in full on the one year anniversary of the conversion date. Interest payments are payable monthly and accrue interest at the rate per annum equal to one-month LIBOR plus 4.0%. The balance of the obligation may be prepaid at any time. At March 31, 2018, the outstanding balance of the Fannie Mae Financing was \$15.0 million and was secured by \$71.4 million of mortgage servicing rights.

During 2018, with the earn-out ending on December 31, 2017, we paid the remaining \$554 thousand in contingent consideration payments related to the CCM acquisition for the fourth quarter of 2017.

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

It is important for us to sell or securitize the loans we originate and, when doing so, maintain the option to also sell the related MSRs associated with these loans. Some investors of ours have raised concerns about the high prepayment speeds of our loans and this has resulted and could further result in adverse pricing or delays in our ability to

Table of Contents

sell or securitize loans and related MSR's on a timely and profitable basis. In the fourth quarter of 2017, we expanded our investor base for loans eligible for sale to Fannie Mae to include additional whole loan investors. In the first and second quarters of 2018, we successfully completed servicing released loan sales to these investors and expect to continue to utilize this alternative exit strategy for Fannie Mae eligible loans. We remain an approved Seller and Servicer in good standing with Fannie Mae.

We believe that current cash balances, cash flows from our mortgage lending operations, the sale of mortgage servicing rights, real estate services fees generated from our long-term mortgage portfolio, and residual interest cash flows from our long-term mortgage portfolio are adequate for our current operating needs. We believe the mortgage and real estate services market is volatile, highly competitive and subject to increased regulation. Competition in mortgage lending comes primarily from mortgage bankers, commercial banks, credit unions and other finance companies which operate in our market area as well as throughout the United States. We compete for loans principally on the basis of the interest rates and loan fees we charge, the types of loans we originate and the quality of services we provide to borrowers, brokers and sellers. Additionally, performance of the long-term mortgage portfolio is subject to the current real estate market and economic conditions. Cash flows from our residual interests in securitizations are sensitive to delinquencies, defaults and credit losses associated with the securitized loans. Losses in excess of current estimates will reduce the residual interest cash receipts from our long-term mortgage portfolio.

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

Critical Accounting Policies

We define critical accounting policies as those that are important to the portrayal of our financial condition and results of operations. Our critical accounting policies require management to make difficult and complex judgments that rely on estimates about the effect of matters that are inherently uncertain due to the effect of changing market conditions and/or consumer behavior. In determining which accounting policies meet this definition, we considered our policies with respect to the valuation of our assets and liabilities and estimates and assumptions used in determining those valuations. We believe the most critical accounting issues that require the most complex and difficult judgments and that are particularly susceptible to significant change to our financial condition and results of operations include those issues included in Management's Discussion and Analysis of Results of Operations in IMH's report on Form 10-K for the year ended December 31, 2017. Such policies have not changed during 2018.

Table of Contents

Financial Condition and Results of Operations

Financial Condition

As of March 31, 2018 compared to December 31, 2017

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

| | March 31, 2018 | December 31, 2017 | Increase (Decrease) | % Change | |
|--|-------------------|----------------------|------------------------|-------------|---|
| ASSETS | | | | | |
| Cash | \$ 29,485 | \$ 33,223 | \$ (3,738) | (11) | % |
| Restricted cash | 5,704 | 5,876 | (172) | (3) | |
| Mortgage loans held-for-sale | 655,506 | 568,781 | 86,725 | 15 | |
| Finance receivables | 26,989 | 41,777 | (14,788) | (35) | |
| Mortgage servicing rights | 174,067 | 154,405 | 19,662 | 13 | |
| Securitized mortgage trust assets | 3,524,053 | 3,670,550 | (146,497) | (4) | |
| Goodwill | 104,587 | 104,587 | — | — | |
| Intangibles, net | 20,532 | 21,582 | (1,050) | (5) | |
| Loans eligible for repurchase from Ginnie Mae | 54,632 | 47,697 | 6,935 | 15 | |
| Other assets | 27,379 | 33,222 | (5,843) | (18) | |
| Total assets | \$ 4,622,934 | \$ 4,681,700 | \$ (58,766) | (1) | % |
| LIABILITIES & EQUITY | | | | | |
| Warehouse borrowings | \$ 650,342 | \$ 575,363 | \$ 74,979 | 13 | % |
| MSR financings | 45,000 | 35,133 | 9,867 | n/a | |
| Convertible notes | 24,977 | 24,974 | 3 | 0 | |
| Contingent consideration | — | 554 | (554) | (100) | |
| Long-term debt (Par value; \$62,000) | 45,337 | 44,982 | 355 | 1 | |
| Securitized mortgage trust liabilities | 3,508,477 | 3,653,265 | (144,788) | (4) | |
| Liability for loans eligible for repurchase from Ginnie Mae | 54,632 | 47,697 | 6,935 | 15 | |
| Repurchase reserve | 5,452 | 6,020 | (568) | (9) | |
| Other liabilities | 28,518 | 28,565 | (47) | (0) | |
| Total liabilities | 4,362,735 | 4,416,553 | (53,818) | (1) | |
| Total equity | 260,199 | 265,147 | (4,948) | (2) | |
| Total liabilities and stockholders' equity | \$ 4,622,934 | \$ 4,681,700 | \$ (58,766) | (1) | % |
| Book value per share | \$ 12.42 | 12.66 | (0.24) | (2) | % |

At March 31, 2018, cash decreased \$3.7 million from \$33.2 million at December 31, 2017. Cash balances decreased primarily due to the payment of operating expenses, \$3.0 million increase in warehouse haircuts (difference between loan balance funded and amount advanced by warehouse lender) associated with the increase in mortgage loans held-for-sale (LHFS) and a \$554 thousand earn-out payments to CashCall Inc. based upon CCM earnings for the fourth quarter of 2017. Partially offsetting the decrease in cash was \$9.9 million in net borrowings under the MSR financing facilities and \$1.8 million in residual cash flows.

LHFS increased \$86.7 million to \$655.5 million at March 31, 2018 as compared to \$568.8 million at December 31, 2017. The increase was due to \$1.3 billion in originations during the first quarter of 2018 partially offset by \$1.2 billion in loan sales. As a normal course of our origination and sales cycle, loans held-for-sale at the end of any period are generally sold within one or two subsequent months.

Table of Contents

Finance receivables decreased \$14.8 million to \$27.0 million at March 31, 2018 as compared to \$41.8 million at December 31, 2017. The decrease was primarily due to \$165.7 million in fundings offset by \$179.9 million in settlements during the quarter ended March 31, 2018.

MSRs increased \$19.7 million to \$174.1 million at March 31, 2018 as compared to \$154.4 million at December 31, 2017. The increase was due to servicing retained loan sales of \$974.7 million in UPB as well as a mark-to-market increase in fair value of \$9.2 million. At March 31, 2018, we serviced \$16.8 billion in UPB for others as compared to \$16.3 billion at December 31, 2017.

As part of the CCM acquisition, we recorded goodwill of \$104.6 million, which is evaluated on a quarterly basis for impairment. Prior to the fourth quarter of 2017, the estimated fair value of CCM substantially exceeded its carrying value. As of December 31, 2017 and March 31, 2018, the estimated fair value of CCM did not substantially exceed its carrying value. The significant assumptions in the assessment include expected future origination levels and expected future gain on sale margins. CCM is a consumer direct call center that provides residential mortgages. Given that the mortgage industry often fluctuates with prevailing interest rates, the mortgage origination market is inherent with uncertainty. In addition, the ongoing dynamic mortgage compliance landscape contributes to the uncertainty of the mortgage market. Each of these factors can have an affect on expected mortgage origination volumes as well as the gain on sale margins which generally tend to follow origination volumes, more originations means higher margins, lower originations mean lower margins. Given the macroeconomic environment that exists today, it is difficult to predict volumes and margins into the future. If our assumptions are not correct, it is possible that an assessment of the estimated fair value of CCM will not exceed its carrying value in the future, in which case impairment of goodwill will be recorded.

Warehouse borrowings increased \$75.0 million to \$650.3 million at March 31, 2018 as compared to \$575.4 million at December 31, 2017. The increase was due to an increase in LHFS at March 31, 2018. We increased our total borrowing capacity to \$1.1 billion from \$960.0 million at December 31, 2017.

We have separate Agreements with two lenders providing for MSR financing facilities of up to \$50.0 million and \$40.0 million. The \$50.0 million facility allows us to borrow up to 55% of the fair market value of Freddie Mac pledged mortgage servicing rights. The \$40.0 million facility allows us to borrow up to 55% of the fair market value of Fannie Mae pledged mortgage servicing rights. At March 31, 2018, the balance outstanding on the Freddie Mac and Fannie Mae facilities was \$30.0 million and \$15.0 million, respectively.

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

| March 31, 2018 | December 31, 2017 | Increase (Decrease) | % Change |
|-------------------|----------------------|------------------------|-------------|
|-------------------|----------------------|------------------------|-------------|

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

| | | | | | |
|---------------------------------------|--------------|--------------|--------------|------|---|
| Securitized mortgage collateral | \$ 3,513,901 | \$ 3,662,008 | \$ (148,107) | (4) | % |
| Other trust assets | 10,152 | 8,542 | 1,610 | 19 | |
| Total trust assets | 3,524,053 | 3,670,550 | (146,497) | (4) | |
| Securitized mortgage borrowings | \$ 3,508,477 | \$ 3,653,265 | \$ (144,788) | (4) | % |
| Total trust liabilities | 3,508,477 | 3,653,265 | (144,788) | (4) | |
| Residual interests in securitizations | \$ 15,576 | \$ 17,285 | \$ (1,709) | (10) | % |

We receive cash flows from our residual interests in securitizations to the extent they are available after required distributions to bondholders and maintaining specified overcollateralization levels and other specified parameters (such as maximum delinquency and cumulative default) within the trusts. The estimated fair value of the residual interests, represented by the difference in the fair value of total trust assets and total trust liabilities, was \$15.6 million at March 31, 2018 as compared to \$17.3 million at December 31, 2017.

We update our collateral assumptions quarterly based on recent delinquency, default, prepayment and loss experience. Additionally, we update the forward interest rates and investor yield (discount rate) assumptions based on information derived from market participants. During the three months ended March 31, 2018, actual losses were relatively flat and were in line with forecasted losses for the majority of trusts with residual value. Principal payments

Table of Contents

and liquidations of securitized mortgage collateral and securitized mortgage borrowings also contributed to the reduction in trust assets and liabilities. The decrease in residual fair value at March 31, 2018 was the result of an increase in forward LIBOR as well as an increase in residual cash flows during the quarter.

- The estimated fair value of securitized mortgage collateral decreased \$148.1 million during the three months ended March 31, 2018, primarily due to reductions in principal from borrower payments and transfers of loans to Real Estate Owned (REO) for single-family and multi-family collateral. Additionally, other trust assets increased \$1.6 million during the three months ended March 31, 2018, primarily due to an increase of \$4.8 million in REO from foreclosures and a \$2.2 million increase in the net realizable value (NRV) of REO. Partially offsetting the increase was REO liquidations of \$5.4 million.
- The estimated fair value of securitized mortgage borrowings decreased \$144.8 million during the three months ended March 31, 2018, primarily due to reductions in principal balances from principal payments during the period for single-family and multi-family collateral as well as a decrease in loss assumptions.

To estimate fair value of the assets and liabilities within the securitization trusts each reporting period, management uses an industry standard valuation and analytical model that is updated monthly with current collateral, real estate, derivative, bond and cost (servicer, trustee, etc.) information for each securitization trust. We employ an internal process to validate the accuracy of the model as well as the data within this model. We use the valuation model to generate the expected cash flows to be collected from the trust assets and the expected required bondholder distribution (trust liabilities). To the extent that the trusts are over collateralized, we may receive the excess interest as the holder of the residual interest. The information above provides us with the future expected cash flows for the securitized mortgage collateral, real estate owned, securitized mortgage borrowings, derivative assets/liabilities, and the residual interests.

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

The following table presents changes in the trust assets and trust liabilities for the three months ended March 31, 2018:

TRUST
LIABILITIES

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

| | Level 3 Recurring Fair Value Measurement | NRV (1) Real estate owned | Total trust assets | Level 3 Recurring Fair Value Measurement Securitized mortgage borrowings | Net trust assets |
|--|--|------------------------------------|-----------------------|--|------------------------|
| Recorded book value at December 31, 2017 | \$ 3,662,008 | \$ 8,542 | \$ 3,670,550 | \$ (3,653,265) | \$ 17,285 |
| Total gains/(losses) included in earnings: | | | | | |
| Interest income | 5,688 | — | 5,688 | — | 5,688 |
| Interest expense | — | — | — | (20,080) | (20,080) |
| Change in FV of net trust assets, excluding REO (2) | (32,755) | — | (32,755) | 28,424 | (4,331) |
| Gains from REO – not at FV but at NRV (2) | — | 2,193 | 2,193 | — | 2,193 |
| Total gains (losses) included in earnings | (27,067) | 2,193 | (24,874) | 8,344 | (16,530) |
| Transfers in and/or out of level 3 | — | — | — | — | — |
| Purchases, issuances and settlements | (121,040) | (583) | (121,623) | 136,444 | 14,821 |
| Recorded book value at March 31, 2018 | \$ 3,513,901 | \$ 10,152 | \$ 3,524,053 | \$ (3,508,477) | \$ 15,576 |

(1) Accounted for at net realizable value.

(2) Represents change in fair value of net trust assets, including trust REO (losses) gains in the consolidated statements of operations for the three months ended March 31, 2018.

Inclusive of gains from REO, total trust assets above reflect a net loss of \$30.6 million for the three months ended March 31, 2018 as a result of a decrease in fair value from securitized mortgage collateral of \$32.8 million

Table of Contents

partially offset by gains from REO of \$2.2 million. Net gains on trust liabilities were \$28.4 million from the decrease in fair value of securitized mortgage borrowings. As a result, non-interest income—net trust assets totaled a decrease of \$2.1 million for the three months ended March 31, 2018.

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

| | March 31, 2018 | | December 31, 2017 | |
|--|-------------------|---|----------------------|---|
| Net trust assets | \$ 15,576 | | \$ 17,285 | |
| Total trust assets | 3,524,053 | | 3,670,550 | |
| Net trust assets as a percentage of total trust assets | 0.44 | % | 0.47 | % |

For the three months ended March 31, 2018, the estimated fair value of the net trust assets decreased slightly as a percentage of total trust assets. The decrease was primarily due to an increase in forward LIBOR as well as cash received.

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

The following tables present the estimated fair value of our residual interests, by securitization vintage year, and other related assumptions used to derive these values at March 31, 2018 and December 31, 2017:

| Origination Year | Estimated Fair Value of Residual Interests by Vintage Year at March 31, 2018 | | | Estimated Fair Value of Residual Interests by Vintage Year at December 31, 2017 | | |
|-------------------------------|--|----------|-----------|---|----------|-----------|
| | SF | MF | Total | SF | MF | Total |
| 2002-2003 (1) | \$ 8,168 | \$ 646 | \$ 8,814 | \$ 8,311 | \$ 663 | \$ 8,974 |
| 2004 | 1,764 | 737 | 2,501 | 2,041 | 970 | 3,011 |
| 2005 | 13 | 8 | 21 | 54 | 85 | 139 |
| 2006 | — | 4,240 | 4,240 | — | 5,161 | 5,161 |
| Total | \$ 9,945 | \$ 5,631 | \$ 15,576 | \$ 10,406 | \$ 6,879 | \$ 17,285 |
| Weighted avg. prepayment rate | 8.0 % | 7.6 % | 7.9 % | 8.0 % | 7.2 % | 7.9 % |
| Weighted avg. discount rate | 16.8 % | 18.0 % | 17.2 % | 17.0 % | 18.0 % | 17.4 % |

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

We utilize a number of assumptions to value securitized mortgage collateral, securitized mortgage borrowings and residual interests. These assumptions include estimated collateral default rates and loss severities (credit losses), collateral prepayment rates, forward interest rates and investor yields (discount rates). We use the same collateral assumptions for securitized mortgage collateral and securitized mortgage borrowings as the collateral assumptions determine collateral cash flows which are used to pay interest and principal for securitized mortgage borrowings and excess spread, if any, to the residual interests. However, we use different investor yield (discount rate) assumptions for

securitized mortgage collateral and securitized mortgage borrowings and the discount rate used for residual interests based on underlying collateral characteristics, vintage year, assumed risk and market participant assumptions. The increase in the estimated fair value of the 2006 multi-family residual interests was due to a reduction in future loss assumptions and recoveries within certain trusts.

Table of Contents

The table below reflects the estimated future credit losses and investor yield requirements for trust assets by product (SF and MF) and securitization vintage at March 31, 2018:

| | Estimated Future Losses (1) | | Investor Yield Requirement (2) | | | |
|-----------|-----------------------------|----|--------------------------------|-----|----|----|
| | SF | MF | SF | MF | SF | MF |
| 2002-2003 | 5 % | * | (3) 6 % | 7 % | | |
| 2004 | 6 | * | (3) 5 | 5 | | |
| 2005 | 8 | * | (3) 4 | 4 | | |
| 2006 | 15 | * | (3) 5 | 4 | | |
| 2007 | 8 | * | (3) 6 | 3 | | |

(1) Estimated future losses derived by dividing future projected losses by UPB at March 31, 2018.

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

(3) Represents less than 1%.

Despite the increase in housing prices through March 31, 2018, housing prices in many parts of the country are still at levels which have significantly reduced or eliminated equity for loans originated after 2003. Future loss estimates are significantly higher for mortgage loans included in securitization vintages after 2005 which reflect severe home price deterioration and defaults experienced with mortgages originated during these periods.

Long-Term Mortgage Portfolio Credit Quality

We use the Mortgage Bankers Association (MBA) method to define delinquency as a contractually required payment being 30 or more days past due. We measure delinquencies from the date of the last payment due date in which a payment was received. Delinquencies for loans 60 days delinquent or greater, foreclosures and delinquent bankruptcies were \$797.1 million or 19.2% of the long-term mortgage portfolio as of March 31, 2018 as compared to \$821.8 million or 19.1% at December 31, 2017.

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

| | March 31, 2018 | Total Collateral | December 31, 2017 | Total Collateral |
|----------------------------------|-------------------|---------------------|----------------------|---------------------|
| Securitized mortgage collateral | | | | |
| 60 - 89 days delinquent | \$ 97,513 | 2.3 % | \$ 112,188 | 2.6 % |
| 90 or more days delinquent | 332,295 | 8.0 | 336,525 | 7.8 |
| Foreclosures (1) | 170,309 | 4.1 | 174,871 | 4.1 |
| Delinquent bankruptcies (2) | 197,030 | 4.7 | 198,212 | 4.6 |
| Total 60 or more days delinquent | \$ 797,147 | 19.2 | \$ 821,796 | 19.1 |
| Total collateral | \$ 4,154,084 | 100.0 | \$ 4,301,316 | 100.0 |

- (1) Represents properties in the process of foreclosure.
- (2) Represents bankruptcies that are 30 days or more delinquent.

Table of Contents

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

| | March 31, 2018 | Total Collateral % | | December 31, 2017 | Total Collateral % | |
|--|-------------------|--------------------------|---|----------------------|--------------------------|---|
| 90 or more days delinquent, foreclosures and delinquent bankruptcies | \$ 699,634 | 16.8 | % | \$ 709,608 | 16.5 | % |
| Real estate owned | 10,152 | 0.2 | | 8,542 | 0.2 | |
| Total non-performing assets | \$ 709,786 | 17.0 | | \$ 718,150 | 16.7 | |

Non-performing assets consist of non-performing loans (mortgages that are 90 or more days delinquent, including loans in foreclosure and delinquent bankruptcies) plus REO. It is our policy to place a mortgage on nonaccrual status when it becomes 90 days delinquent and to reverse from revenue any accrued interest, except for interest income on securitized mortgage collateral when the scheduled payment is received from the servicer. The servicers are required to advance principal and interest on loans within the securitization trusts to the extent the advances are considered recoverable. IFC, a subsidiary of IMH and master servicer, may be required to advance funds, or in most cases cause the loan servicers to advance funds, to cover principal and interest payments not received from borrowers depending on the status of their mortgages. As of March 31, 2018, non-performing assets (UPB of loans 90 or more days delinquent, foreclosures and delinquent bankruptcies plus REO) as a percentage of the total collateral was 17.0%. At December 31, 2017, non-performing assets to total collateral was 16.7%. Non-performing assets decreased by approximately \$8.4 million at March 31, 2018 as compared to December 31, 2017. At March 31, 2018, the estimated fair value of non-performing assets (representing the fair value of loans 90 or more days delinquent, foreclosures and delinquent bankruptcies plus REO) was \$197.6 million or 4.3% of total assets. At December 31, 2017, the estimated fair value of non-performing assets was \$212.7 million or 4.5% of total assets.

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

For the three months ended March 31, 2018 and 2017, we recorded an increases in net realizable value of REO in the amount of \$2.2 million and \$1.5 million, respectively. Increases of the net realizable value reflect increases in value of the REO subsequent to foreclosure date, but prior to the date of sale.

The following table presents the balances of REO:

| | March 31, 2018 | December 31, 2017 |
|----------------|-------------------|----------------------|
| REO | \$ 14,936 | \$ 15,519 |
| Impairment (1) | (4,784) | (6,977) |
| Total | \$ 10,152 | \$ 8,542 |

(1) Impairment represents the cumulative write-downs of net realizable value subsequent to foreclosure.

In calculating the cash flows to assess the fair value of the securitized mortgage collateral, we estimate the future losses embedded in our loan portfolio. In evaluating the adequacy of these losses, management takes many factors into consideration. For instance, a detailed analysis of historical loan performance data is accumulated and reviewed. This data is analyzed for loss performance and prepayment performance by product type, origination year and securitization issuance. The data is also broken down by collection status. Our estimate of losses for these loans is developed by estimating both the rate of default of the loans and the amount of loss severity in the event of default. The rate of default is assigned to the loans based on their attributes (e.g., original loan-to-value, borrower credit score, documentation type, geographic location, etc.) and collection status. The rate of default is based on analysis of migration

Table of Contents

of loans from each aging category. The loss severity is determined by estimating the net proceeds from the ultimate sale of the foreclosed property. The results of that analysis are then applied to the current mortgage portfolio and an estimate is created. We believe that pooling of mortgages with similar characteristics is an appropriate methodology in which to evaluate the future loan losses.

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

Results of Operations

For the Three Months Ended March 31, 2018 compared to the Three Months Ended March 31, 2017

| | For the Three Months Ended March 31, | | Increase (Decrease) | % Change | |
|--|--------------------------------------|-----------|------------------------|-------------|---|
| | 2018 | 2017 | | | |
| Revenues | \$ 40,125 | \$ 45,342 | \$ (5,217) | (12) | % |
| Expenses (1) | (35,748) | (44,557) | 8,809 | 20 | |
| Net interest income | 1,020 | 446 | 574 | 129 | |
| Change in fair value of long-term debt | 1,224 | (2,497) | 3,721 | 149 | |
| Change in fair value of net trust assets, including trust | | | | | |
| REO gains (losses) | (2,138) | 6,319 | (8,457) | (134) | |
| Income tax expense | (610) | (426) | (184) | (43) | |
| Net earnings | \$ 3,873 | \$ 4,627 | \$ (754) | (16) | |
| Earnings per share available to common stockholders—basic | \$ 0.18 | \$ 0.29 | \$ (0.10) | (36) | % |
| Earnings per share available to common stockholders—diluted | \$ 0.18 | \$ 0.29 | \$ (0.11) | (37) | % |

(1) Includes changes in contingent consideration liability resulting in expense of \$0.5 million for the three months ended March 31, 2017.

Revenues

| | For the Three Months Ended March 31, | | Increase (Decrease) | % Change | |
|---|--------------------------------------|-----------|------------------------|-------------|---|
| | 2018 | 2017 | | | |
| Gain on sale of loans, net | \$ 21,482 | \$ 37,319 | \$ (15,837) | (42) | % |
| Servicing fees, net | 9,463 | 7,320 | 2,143 | 29 | |
| Gain (loss) on mortgage servicing rights, net | 7,705 | (977) | 8,682 | 889 | |
| Real estate services fees, net | 1,385 | 1,633 | (248) | (15) | |
| Other revenues | 90 | 47 | 43 | 91 | |

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

| | | | | | |
|----------------|-----------|-----------|------------|------|---|
| Total revenues | \$ 40,125 | \$ 45,342 | \$ (5,217) | (12) | % |
|----------------|-----------|-----------|------------|------|---|

Gain on sale of loans, net. For the three months ended March 31, 2018, gain on sale of loans, net totaled \$21.5 million compared to \$37.3 million in the comparable 2017 period. The \$15.8 million decrease is primarily due to a \$10.1 million increase in mark-to-market losses on LHFS, an \$8.9 million decrease in premiums from the sale of mortgage loans, a \$1.6 million decrease in premiums from servicing retained loan sales, a \$3.2 million increase in direct loan origination expenses and a \$2.0 million increase in provision for repurchases. Partially offsetting the decrease in gain on sale of loans, net was a \$10.0 million increase in realized and unrealized net gains on derivative financial instruments.

Table of Contents

The overall decrease in gain on sale of loans, net was primarily due to a 16% decrease in volume as well as a decrease in gain on sale margins. For the three months ended March 31, 2018, we originated and sold \$1.3 billion and \$1.2 billion of loans, respectively, as compared to \$1.6 billion and \$1.5 billion of loans originated and sold, respectively, during the same period in 2017. Margins decreased to approximately 163 bps for the three months ended March 31, 2018 as compared to 236 bps for the same period in 2017. The increase in interest rates during the quarter as compared to the first quarter of 2017, as well as an increase in direct origination expenses as a result of an increase in competition for volume were the primary drivers in margin compression.

Servicing fees, net. For the three months ended March 31, 2018, servicing fees, net was \$9.5 million compared to \$7.3 million in the comparable 2017 period. The increase in servicing fees, net was the result of the servicing portfolio increasing 28% to an average balance of \$16.6 billion for the three months ended March 31, 2018 as compared to an average balance of \$13.0 billion for the three months ended March 31, 2017. The increase in the average balance of the servicing portfolio is a result of our efforts during the past year to retain servicing. During the three months ended March 31, 2018, we had \$974.7 million in servicing retained loan sales.

Gain (loss) on mortgage servicing rights, net.

| | For the Three Months Ended March 31, | | | % Change |
|---|--------------------------------------|------------|------------------------|-------------|
| | 2018 | 2017 | Increase (Decrease) | |
| Realized and unrealized gains (losses) from hedging instruments | \$ (1,473) | \$ 559 | \$ (2,032) | (364) |
| Loss on sale of mortgage servicing rights | (2) | (414) | 412 | 100 |
| Changes in fair value: | | | | |
| Due to changes in valuation market rates, inputs or assumptions | 16,200 | 3,108 | 13,092 | 421 |
| Other changes in fair value: | | | | |
| Scheduled principal prepayments | (3,108) | (1,705) | (1,403) | (82) |
| Voluntary prepayments | (3,912) | (2,525) | (1,387) | (55) |
| Total changes in fair value | \$ 9,180 | \$ (1,122) | \$ 10,302 | 918 |
| Gain (loss) on mortgage servicing rights, net | \$ 7,705 | \$ (977) | \$ 8,682 | 889 |

For the three months ended March 31, 2018, gain (loss) on MSR, net was a gain of \$7.7 million compared to a loss of \$977 thousand in the comparable 2017 period. For the three months ended March 31, 2018, we recorded an \$9.2 million gain from a change in fair value of MSR primarily the result of mark-to-market changes related to an increase in interest rates resulting in a reduction in prepayment speeds partially offset by an increase in scheduled and voluntary prepayments. Partially offsetting the gain was \$1.5 million in realized and unrealized losses from hedging instruments related to MSR.

Real estate services fees, net. For the three months ended March 31, 2018, real estate services fees, net were \$1.4 million compared to \$1.6 million in the comparable 2017 period. The \$201 thousand decrease was primarily the result of a decrease in transactions related to the decline in the number of loans and the UPB of the long-term mortgage portfolio as compared to 2017.

Expenses

| | For the Three Months Ended March 31, | | | |
|--|--------------------------------------|-----------|------------------------|-------------|
| | 2018 | 2017 | Increase (Decrease) | % Change |
| Personnel expense | \$ 17,742 | \$ 24,919 | \$ (7,177) | (29) % |
| Business promotion | 9,731 | 10,231 | (500) | (5) |
| General, administrative and other | 8,275 | 8,023 | 252 | 3 |
| Accretion of contingent consideration | — | 845 | (845) | (100) |
| Change in fair value of contingent consideration | — | 539 | (539) | (100) |
| Total expenses | \$ 35,748 | \$ 44,557 | \$ (8,809) | (20) % |

Total expenses were \$35.7 million for the three months ended March 31, 2018, compared to \$44.6 million for the comparable period of 2017. Personnel expense decreased \$7.2 million to \$17.7 million for the three months ended

Table of Contents

March 31, 2018. The decrease is primarily related to staff reduction in the first quarter of 2018 as well as a reduction in commission expense due to a decrease in loan originations. As a result of the reduction in loan origination volumes, we continue to reduce overhead to more closely align staffing levels to origination volumes in the current economic environment. As a result of the staff reductions in the first quarter of 2018, average headcount decreased 20% for the first quarter of 2018 as compared to the same period in 2017.

Business promotion decreased \$500 thousand to \$9.7 million for the three months ended March 31, 2018. During the first quarter of 2018, business promotion decreased as compared to 2017 despite efforts to increase NonQM and purchase money production with the reduction in refinance activity as a result of the increase in interest rates. Our centralized call center purchases leads and promotes its business through radio and television advertisements.

General, administrative and other expenses increased to \$8.3 million for the three months ended March 31, 2018, compared to \$8.0 million for the same period in 2017. The increase was primarily related to a \$640 thousand increase in legal and professional fees associated with defending litigation matters. Partially offsetting the increase was a \$155 thousand decrease in occupancy expense, a \$133 thousand decrease in premises and equipment expense and a \$100 thousand decrease in other general and administrative expenses.

As part of the acquisition of CCM, we recorded accretion and change in fair value of the contingent consideration liability from the close of the transaction in March 2015 through the end of the earn-out period in December 2017.

With the end of the earn-out period in December 2017 and the final contingent consideration payment in the first quarter of 2018, we have no contingent consideration liability. However, we continue to record goodwill of \$104.6 million, and intangible assets, net of \$20.5 million. Goodwill is evaluated on a quarterly basis for impairment while the intangible assets are amortized over the useful lives of the various intangible assets.

Net Interest Income (Expense)

We earn net interest income primarily from mortgage assets, which include securitized mortgage collateral, loans held-for-sale and finance receivables, or collectively, "mortgage assets," and, to a lesser extent, interest income earned on cash and cash equivalents. Interest expense is primarily interest paid on borrowings secured by mortgage assets, which include securitized mortgage borrowings and warehouse borrowings and to a lesser extent, interest expense paid on long-term debt, Convertible Notes, MSR Financing and Term Financing. Interest income and interest expense during the period primarily represents the effective yield, based on the fair value of the trust assets and liabilities.

The following tables summarize average balance, interest and weighted average yield on interest-earning assets and interest-bearing liabilities, for the periods indicated. Cash receipts and payments on derivative instruments hedging

Table of Contents

interest rate risk related to our securitized mortgage borrowings are not included in the results below. These cash receipts and payments are included as a component of the change in fair value of net trust assets.

| | For the Three Months Ended March 31, 2018 | | | 2017 | | |
|------------------------------------|--|-----------|--------|--------------------|-----------|--------|
| | Average Balance | Interest | Yield | Average Balance | Interest | Yield |
| ASSETS | | | | | | |
| Securitized mortgage collateral | \$ 3,587,954 | \$ 43,137 | 4.81 % | \$ 3,962,613 | \$ 57,921 | 5.85 % |
| Mortgage loans held-for-sale | 566,684 | 6,617 | 4.67 | 283,314 | 3,199 | 4.52 |
| Finance receivables | 23,083 | 382 | 6.62 | 28,511 | 428 | 6.00 |
| Other | 31,597 | 14 | 0.18 | 36,939 | 36 | 0.39 |
| Total interest-earning assets | \$ 4,209,318 | \$ 50,150 | 4.77 | \$ 4,311,377 | \$ 61,584 | 5.71 |
| LIABILITIES | | | | | | |
| Securitized mortgage borrowings | \$ 3,580,871 | \$ 40,958 | 4.58 | \$ 3,955,136 | \$ 55,811 | 5.64 % |
| Warehouse borrowings (1) | 577,962 | 6,125 | 4.24 | 305,035 | 2,981 | 3.91 |
| MSR financing facilities | 34,047 | 497 | 5.84 | 19,518 | 242 | 4.96 |
| Long-term debt | 45,159 | 1,069 | 9.47 | 48,626 | 1,219 | 10.03 |
| Convertible notes | 24,966 | 471 | 7.55 | 24,963 | 471 | 7.55 |
| Term financing | — | — | — | 13,619 | 407 | 11.95 |
| Other | 245 | 10 | 16.33 | 570 | 7 | 4.91 |
| Total interest-bearing liabilities | \$ 4,263,250 | \$ 49,130 | 4.61 | \$ 4,367,467 | \$ 61,138 | 5.60 |
| Net Interest Spread (2) | | \$ 1,020 | 0.16 % | | \$ 446 | 0.11 % |
| Net Interest Margin (3) | | | 0.10 % | | | 0.04 % |

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

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

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

Net interest spread increased \$574 thousand for the three months ended March 31, 2018 primarily attributable to an increase in the net interest spread between loans held-for-sale and finance receivables and their related warehouse borrowings and a decrease in interest expense related to the payoff of the Term Financing as well as settlement of the Trust Preferred Securities in 2017. Partially offsetting the increase in net spread was an increase in interest expense as a result of the MSR financing facility. As a result, the net interest margin increased to 0.10% for the three months ended March 31, 2018 from 0.04% for the three months ended March 31, 2017.

During the quarter ended March 31, 2018, the yield on interest-earning assets decreased to 4.77% from 5.71% in the comparable 2017 period. The yield on interest-bearing liabilities decreased to 4.61% for the three months ended March 31, 2018 from 5.60% for the comparable 2017 period. In connection with the fair value accounting for securitized mortgage collateral and borrowings and long-term debt, interest income and interest expense is recognized using effective yields based on estimated fair values for these instruments. The decrease in yield for securitized mortgage collateral and securitized mortgage borrowings is primarily related to increased prices on mortgage-backed bonds which resulted in a decrease in yield as compared to the previous period.

Change in the fair value of long-term debt.

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

In the first quarter of 2018, we adopted ASU 2016-01, which effectively bifurcates the market and instrument specific credit risk components of changes in long-term debt. The market portion will continue to be a component of net

Table of Contents

earnings (loss) as the change in fair value of long-term debt, but the instrument specific credit risk portion will be a component of accumulated other comprehensive earnings (loss). During the first quarter of 2018, the fair value of the long-term debt increased by \$215 thousand. The \$215 thousand change was the result of a \$1.4 million change in the instrument specific credit risk partially offset by a \$1.2 million change in the market risk during the quarter.

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

| | For the Three Months Ended March 31, | |
|---|--|----------|
| | 2018 | 2017 |
| Change in fair value of net trust assets, excluding REO | \$ (4,331) | \$ 4,786 |
| Gains from REO | 2,193 | 1,533 |
| Change in fair value of net trust assets, including trust gains | \$ (2,138) | \$ 6,319 |

The change in fair value related to our net trust assets (residual interests in securitizations) was a loss of \$2.1 million for the three months ended March 31, 2018. The change in fair value of net trust assets, excluding REO was due to \$4.3 million in losses from changes in fair value of securitized mortgage borrowings and securitized mortgage collateral primarily associated with an increase in LIBOR, partially offset by updated assumptions on certain later vintage trusts with improved performance. Additionally, the NRV of REO increased \$2.2 million during the period attributed to lower expected loss severities on properties held in the long-term mortgage portfolio during the period.

The change in fair value related to our net trust assets (residual interests in securitizations) was a gain of \$6.3

million for the three months ended March 31, 2017. The change in fair value of net trust assets, including REO was due

to \$4.8 million in gains from changes in fair value of securitized mortgage borrowings and securitized mortgage

collateral primarily associated updated loss assumptions and recoveries on a certain later vintage multifamily trust with

improved performance. Additionally, the NRV of REO increased \$1.5 million during the period as a result of lower expected loss severities on properties held in the long-term mortgage portfolio.

Income Taxes

We recorded income tax expense of \$610 thousand for the three months ended March 31, 2018, primarily the result of state income taxes from states where we do not have net operating loss carryforwards or state minimum taxes, including AMT. For the three months ended March 31, 2017, we recorded income tax expense of \$426 thousand primarily the result of amortization of the deferred charge, federal alternative minimum tax (AMT), and state income taxes from states where we do not have net operating loss carryforwards or state minimum taxes, including AMT.

The deferred charge represented the deferral of income tax expense on inter-company profits that resulted from the sale of mortgages from taxable subsidiaries to IMH prior to 2008. The deferred charge amortization and/or

impairment, which does not result in any tax liability to be paid was calculated based on the change in fair value of the underlying securitized mortgage collateral during the period. At December 31, 2017, the deferred charge was included in other assets in the accompanying consolidated balance sheets and was amortized as a component of income tax expense in the accompanying consolidated statements of operations. With the adoption of ASU 2016-16 on January 1, 2018, the deferred charge was eliminated with a cumulative effect adjustment to opening retained earnings and it will no longer be amortized as a component of income tax expense.

As of December 31, 2017, we had estimated federal net operating loss (NOL) carryforwards of approximately \$619.9 million. Federal net operating loss carryforwards begin to expire in 2027. As of December 31, 2017, we had estimated California NOL carryforwards of approximately \$431.0 million, which begin to expire in 2028. We may not be able to realize the maximum benefit due to the nature and tax entities that holds the NOL

Results of Operations by Business Segment

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

45

Table of Contents

Mortgage Lending

| | For the Three Months Ended March 31, | | | | |
|--|--------------------------------------|-----------|------------------------|-------------|---|
| | 2018 | 2017 | Increase (Decrease) | % Change | % |
| Gain on sale of loans, net | \$ 21,482 | \$ 37,319 | \$ (15,837) | (42) | % |
| Servicing fees, net | 9,463 | 7,320 | 2,143 | 29 | |
| Loss on mortgage servicing rights, net | 7,705 | (977) | 8,682 | 889 | |
| Other | — | 14 | (14) | (100) | |
| Total revenues | 38,650 | 43,676 | (5,026) | (12) | |
| Other income | 334 | 406 | (72) | | |