COMPASS MINERALS INTERNATIONAL INC
Form 4
March 08, 2005

FORM 4

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

STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP OF SECURITIES

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934, Section 17(a) of the Public Utility Holding Company Act of 1935 or Section 30(h) of the Investment Company Act of 1940

OMB APPROVAL

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(Print or Type Responses)

1. Name and Address of Reporting Person *
GOADBY DAVID J

(Last) (First) (Middle)

C/O COMPASS MINERALS INTERNATIONAL, INC., 8300 COLLEGE BLVD

(Street)

OVERLAND PARK, KS 66210

(City) (State) (Zip)

2. Issuer Name **and** Ticker or Trading Symbol
COMPASS MINERALS INTERNATIONAL INC [CMP]

3. Date of Earliest Transaction (Month/Day/Year)
03/07/2005

4. If Amendment, Date Original Filed(Month/Day/Year)

5. Relationship of Reporting Person(s) to Issuer

(Check all applicable)

_____ Director _____ 10% Owner
__X__ Officer (give title below) _____ Other (specify below)
VP and Managing Director

6. Individual or Joint/Group Filing(Check Applicable Line)
_X_ Form filed by One Reporting Person
___ Form filed by More than One Reporting Person

Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned

1.Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)		4. Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)			5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Indirect Beneficial Ownership (Instr. 4)
			Code	V	Amount	(A) or (D)	Price			
Common Stock	03/07/2005		S		1,000	D	$ 25	99,666	D	
Common Stock	03/07/2005		S		14,000	D	$ 24.95	85,666	D	

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

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SEC 1474 (9-02)

Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned
(*e.g.*, puts, calls, warrants, options, convertible securities)

1. Title of Derivative Security (Instr. 3)	2. Conversion or Exercise Price of Derivative Security	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if any (Month/Day/Year)	4. Transaction Code (Instr. 8)		5. Number of Derivative Securities Acquired (A) or Disposed of (D) (Instr. 3, 4, and 5)		6. Date Exercisable and Expiration Date (Month/Day/Year)		7. Title and Amount of Underlying Securities (Instr. 3 and 4)		8. Price of Derivative Security (Instr. 5)	9. Nu Deriv Secur Bene Owne Follo Repo Trans (Instr
				Code	V	(A)	(D)	Date Exercisable	Expiration Date	Title	Amount or Number of Shares		

Reporting Owners

Reporting Owner Name / Address	Relationships			
	Director	10% Owner	Officer	Other
GOADBY DAVID J C/O COMPASS MINERALS INTERNATIONAL, INC. 8300 COLLEGE BLVD OVERLAND PARK, KS 66210			VP and Managing Director	

Signatures

By: /s/ Todd S. Graf as Attorney-in-Fact	03/07/2005
**Signature of Reporting Person	Date

Explanation of Responses:

* If the form is filed by more than one reporting person, *see* Instruction 4(b)(v).

** Intentional misstatements or omissions of facts constitute Federal Criminal Violations. *See* 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).

Note: File three copies of this Form, one of which must be manually signed. If space is insufficient, *see* Instruction 6 for procedure.
Potential persons who are to respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB number. r sale. The Company endeavors to mitigate interest rate risk by attempting to match the rate reset (or repricing) characteristics of its assets with its liabilities. The Company also utilizes forward loan sale commitments to provide liquidity and to hedge its residential mortgage loan pipeline and loans held for sale, as well as interest rate caps to hedge execution of its securitization transactions. The objective of our interest rate and liquidity risk management activities is to reduce the risk of operational disruption and to reduce the volatility in income caused by changes in interest rates; however, the mortgage banking industry is inherently subject to income volatility due to the effect of interest rate variations on loan production volume, premiums realized on loan sales and securitizations, and loan pre-payment patterns, which in turn effects the valuation of the Company's residual interests and mortgage servicing rights, as well as the amount of loan servicing income realized. The Company's two operating lines of business are designed to be somewhat counter-cyclical and to provide balance in varying economic cycles; however, both of the Company's operating businesses are influenced by the overall condition of the economy, in particular the interest rate environment and, as a result, experience cyclicality in volume, loan losses and earnings. The Company

strives to manage its operations so as to optimize operational efficiency and to maintain risks within acceptable parameters. The Company's lending operations generate income as follows: o Commercial real estate loans, which are held for investment, generate net interest income on the difference between the rates charged on the loans and the cost of borrowed funds. An allowance for loan losses is maintained through provisions (expense) that are recognized in the consolidated statements of income. o All of the residential real estate loans originated are currently sold for varying levels of gain through whole loan sales to other financial institutions, and to a lesser degree, to various investors through securitization transactions. A held for sale valuation reserve, a loan repurchase reserve and a premium recapture reserve are maintained through provisions (expense) that are recognized in the 26 consolidated statements of income. This discussion and analysis should be read in conjunction with the Consolidated Financial Statements and Notes thereto presented under Item 1, and the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2003. CRITICAL ACCOUNTING POLICIES AND ESTIMATES The Company's accounting policies are essential to understanding management's discussion and analysis of financial condition and results of operations. The Company has identified three accounting policies as being critical because they require more significant judgment and estimates about matters that may differ from the estimates determined under different assumptions or conditions. These critical accounting policies relate to the gain on whole loan sales and securitizations, allowance for loan losses and income taxes. The critical accounting policies and estimates are further discussed in the Management's Discussion and Analysis in the Annual Report on Form 10-K for the year ended December 31, 2003. RESULTS OF OPERATIONS The Company reported net income from continuing operations of $85,120,000 for the third quarter of 2004. This is compared to net income from continuing operations of $55,493,000 for the third quarter of 2003. For the first nine months of 2004, net income from continuing operations totaled $263,161,000, as compared to $143,856,000 for the first nine months of 2003. The Company reported income before income taxes of $144,898,000 for the third quarter of 2004 as compared to $94,472,000 for the third quarter of 2003. For the first nine months of 2004, income before income taxes totaled $449,640,000, as compared to $244,883,000 for the first nine months of 2003. The increase in income before income taxes for the third quarter and first nine months of 2004 represents increases of 53% and 84%, respectively, over the results for the third quarter and first nine months of 2003. This is primarily a result of increased levels of net interest income and gain on the sale of residential real estate loans and a lower provision for loan losses, partially offset by an increase in non-interest expense. The increases in the gain on sale of residential real estate loans and non-interest expense are both primarily a result of significantly higher levels of residential real estate loan origination volumes, offset by lower gross premiums realized on the sale of the residential real estate loans. 27 NET INTEREST INCOME The following tables identify the consolidated interest income, interest expense, average interest-earning assets and interest-bearing liabilities, and net interest margins, as well as an analysis of changes in net interest income due to volume and rate changes, for the third quarter and first nine months of 2004 and 2003: THREE MONTHS ENDED SEPTEMBER 30, -- 2004 2003 ----------------------------------- ------------------------------- AVERAGE YIELD/ AVERAGE YIELD/ BALANCE INTEREST COST BALANCE INTEREST COST ------------ --------- ------ ---------- --------- ----- (THOUSANDS OF DOLLARS, EXCEPT PERCENTS) Interest-earning assets (1): Commercial real estate loans .... $ 3,819,339 $ 72,405 7.54% $ 3,942,746 $ 77,220 7.77 % Residential real estate loans (2) .... 4,763,213 86,334 7.21% 3,321,231 60,106 7.18 % Syndicated commercial loans .... 3,075 - - 7,291 49 2.67 % Residual interests in securitized loans .... 19,446 856 17.51% 2,267 76 22.66 % Cash equivalents and investment securities ..... 711,122 3,309 1.85% 220,977 993 1.78 % ---------- -------- ------ ---------- --------- ----- Total interest-earning assets .... $ 9,316,195 $ 162,904 6.96% $ 7,494,512 $ 138,444 7.33 % =========== ========= ====== =========== ========= ====== Interest-bearing liabilities: Time deposits .... $ 5,325,285 $ 29,000 2.17% $ 3,796,110 $ 23,293 2.43 % Savings deposits .... 1,774,230 9,038 2.03% 1,452,293 7,109 1.94 % FHLB advances .... 931,239 4,787 2.05% 1,368,837 7,085 2.05 % Warehouse lines of credit .... - 501 - 29,109 176 2.40 % Senior notes due 2004 .... - - - 22,385 440 7.86 % Senior notes due 2009 .... 183,450 3,691 8.05% 190,700 3,836 8.05 % LYONs .... 628 7 4.43% 3,140 40 5.05 % Junior subordinated debentures/preferred securities .... 103,093 2,320 9.00% 100,000 2,250 9.00 % Other .... 11,204 56 1.99% 3,973 (9) (0.90)% ----------- --------- ------ ----------- --------- ----- Total interest-bearing liabilities .... $ 8,329,129 $ 49,400 2.36% $ 6,966,547 $ 44,220 2.52 % =========== ========= ====== =========== ========= ====== Net interest income .... $ 113,504 $ 94,224 ========= ========= Percent of average interest-earning assets: Interest income .... 6.96% 7.33 % Interest expense .... 2.11% 2.34 % ------ ---- Net interest margin .... 4.85% 4.99 % ====== ==== 28 NINE MONTHS ENDED SEPTEMBER 30, -- 2004 2003 ----------------------------------- -------------------------------- AVERAGE YIELD/ AVERAGE YIELD/ BALANCE INTEREST COST BALANCE INTEREST COST ----------- --------- ----- ----------- --------- ----- (THOUSANDS OF DOLLARS, EXCEPT PERCENTS) Interest-earning assets (1): Commercial real estate loans .... $ 3,921,667 $ 221,796 7.55% $ 3,846,399 $ 225,573 7.84% Residential real estate loans (2) .... 5,158,118 269,622 6.98% 2,764,769 154,678 7.48% Syndicated commercial loans .... 4,491 78 2.32% 13,843 149 1.44% Residual interests in securitized loans .... 12,477 2,451 26.24% 2,724 76 18.86% Cash equivalents and investment securities ..... 496,492 6,693 1.80% 234,386 4,779 2.73% ----------- --------- ----- ----------- --------- ----- Total interest-earning assets .... $ 9,593,245 500,640 6.97% 6,862,121 385,255 7.51% =========== ========= ===== =========== ========= ===== Interest-bearing liabilities: Time deposits .... $ 5,240,056 $ 82,184 2.09% $ 3,676,327 $ 73,996 2.69% Savings deposits .... 1,764,570 25,911 1.96% 1,341,291 20,690 2.06% FHLB advances .... 1,435,697 20,535 1.91% 1,033,937 17,920 2.32% Warehouse lines of credit .... - 751 - 9,810 176 2.40% Senior notes due 2004 .... 6,291 372 7.88% 42,586 2,590 8.11% Senior notes due 2009 .... 186,943 11,293 8.05% 190,700 11,510 8.05% LYONs .... 644 24 4.98% 3,129 119 5.08% Junior subordinated debentures/preferred securities .... 103,093 6,959 9.00% 100,000 6,750 9.00% Other .... 9,282 139 2.00% 41,460 339 1.09% ---------- --------- ----- ----------- --------- ----- Total interest-bearing liabilities .... $ 8,746,576 $ 148,168 2.26% $ 6,439,240 $ 134,090 2.78% =========== ========= ===== =========== ========= ===== Net interest income .... $ 352,472 $ 251,165 ========= ========= Percent of average interest-earning assets: Interest income .... 6.97% 7.51% Interest expense .... 2.06% 2.61% ----- ----- Net Interest Margin .... 4.91% 4.90% ===== ===== (1) Average loan balances include non-accrual loan balances. (2) Includes loans held for sale and other. 29 THREE MONTHS ENDED SEPTEMBER 30, NINE MONTHS ENDED SEPTEMBER 30, 2004 COMPARED TO 2003 2004 COMPARED TO 2003 ---------------------------------- ------------------------------------ CHANGE DUE TO CHANGE DUE TO --------------------- ----------------------- VOLUME RATE TOTAL VOLUME RATE TOTAL -------- -------- -------- --------- --------- --------- (THOUSANDS OF DOLLARS) Cash equivalent and investment securities ..... $ 1,617 $ 699 $ 2,316 $ 2,492 $ (578) $ 1,914 Loans Commercial real estate .... (2,339) (2,476) (4,815) 4,257 (8,034) (3,777) Residential real estate .... 26,127 78 26,205 125,019 (10,114) 114,905 Other .... 741 13 754 1,802 541 2,343 -------- -------- -------- --------- -------- --------- Total Loans .... 24,529 (2,385) 22,144 131,078 (17,607) 113,471 -------- -------- -------- --------- -------- --------- Total increase / (decrease) in interest income .... 26,146 (1,686) 24,460 133,570 (18,185) 115,385 -------- -------- -------- --------- -------- --------- Time deposits .... (8,327) 2,620 (5,707) (24,525) 16,337 (8,188) Savings deposits .... (1,640) (289) (1,929) (6,215) 994 (5,221) FHLB advances .... 2,249 49 2,298 (5,746) 3,131 (2,615) Warehouse lines of credit .... - (325) (325) - (575) (575) Senior notes due 2004 and 2009 .... 585 - 585 2,435 - 2,435 LYONs .... 33 - 33 95 - 95 Junior subordinated debentures / preferred securities .... (70) - (70) (209) - (209) Other .... (36) (29) (65) 481 (281) 200 -------- -------- -------- --------- -------- --------- Total increase / (decrease) in interest expense .... (7,206) 2,026 (5,180) (33,684) 19,606 (14,078) -------- -------- -------- --------- -------- --------- Increase in net interest income .... $ 18,940 $ 340 $ 19,280 $ 99,886 $ 1,421 $ 101,307 ======== ======== ======== ========= ======== ========= The Company recorded net interest income for the third quarter of 2004 of $113.5 million as compared to $94.2 million for the third quarter of 2003. For the first nine months of 2004, the Company recorded net interest income of $352.5 million as compared to $251.2 million for the first nine months of 2003. The quarterly and year to date increase in net interest income is primarily a result of an increase in the average interest-earning assets, primarily residential real estate loans. Total average interest-earning assets increased 24% to $9.3 billion during the third quarter of 2004, as compared to $7.5 billion during the third quarter of 2003. The net interest income margin slightly decreased to an annualized 4.85% for the third quarter of 2004 from 4.99% for the third quarter of 2003. Total average interest-earning assets increased 40% to $9.6 billion for the first nine months of 2004, as compared to $6.9 billion during the first nine months of 2003. The net interest income margin also increased slightly to an annualized 4.91% for the first nine months of 2004 from 4.90%

for the first nine months of 2003. Net interest income is impacted by the volume, mix and rate of interest-earning assets and interest-bearing liabilities. The decrease in the Company's quarterly net interest margin is due primarily to a higher average liquidity position at FIL during the third quarter of 2004. PROVISION FOR LOAN LOSSES The provision for loan losses was reversed (or credited) in the amount of $10.3 million during the third quarter of 2004 as compared to a $29.4 million provision for the third quarter of 2003. As a result, there was also a significant decrease in the provision for loan losses to $6.2 million for the first nine months 30 of 2004 as compared to $79.9 million for the first nine months of 2003. The reversal in the provision for loan losses during the third quarter was primarily a result of the transfer of the residential real estate loans held for investment to loans held for sale. In addition, the overall decrease in the amount of provision for loan losses in 2004 is attributable to a lower level of net loan charge-offs, non-accrual loans and loans held for investment in its commercial real estate lending operation. Management believes that the allowance for loan losses is adequate to cover the inherent risks within the loans held for investment at September 30, 2004. NON-INTEREST INCOME The gain on the sale of residential real estate loans increased from $83.7 million in the third quarter of 2003 to $89.4 million for the third quarter of 2004. For the first nine months of 2004, the gain on the sale of residential real estate loans increased to $338.6 million, as compared to $211.6 million for the first nine months of 2003. This increase is attributable to a significant increase in the volume of loans sold, partially offset by the realization of lower premiums on the loans sold, in the third quarter and first nine months of 2004, as compared to the third quarter and first nine months of 2003. A total of $6.80 billion in loans were sold (including loans sold via securitization) during the third quarter of 2004, as compared to loan sales of $2.78 billion during the third quarter of 2003. For the first nine months of 2004, a total of $16.60 billion in loans were sold (including loans sold via securitization), as compared to loan sales of $7.31 billion during the first nine months of 2003. The average gross premium on loans sold during the third quarter of 2004 was 3.02% as compared to an average of 4.42% for the third quarter of 2003. For the first nine months of 2004, the average gross premium on loans sold was 3.68% as compared to an average of 4.39% for the first nine months of 2003. Such premiums have exhibited, and are expected to continue to exhibit, variability (often significant) based on various economic and interest rate environments. The gain percentage on these sales decreased from 3.01% in the third quarter of 2003 to 1.32% in the third quarter of 2004. For the first nine months of 2004, the gain percentage on these sales decreased to 2.02%, as compared to 2.89% in the first nine months of 2003. The following tables provide the amounts of loans sold during the respective periods and additional detail on the gain on sale (thousands of dollars): THREE MONTHS ENDED NINE MONTHS ENDED SEPTEMBER 30, SEPTEMBER 30, -------------------------- ---------------------------- 2004 2003 2004 2003 ----------- ----------- ------------ ----------- Loan sales (net of repurchases): Whole loan .... $ 6,245,154 $ 2,222,260 $ 14,426,043 $ 6,751,860 Securitization .... 555,814 561,577 2,178,572 561,577 ----------- ----------- ------------ ----------- $ 6,800,968 $ 2,783,837 $ 16,604,615 $ 7,313,437 =========== =========== ============ =========== 31 THREE MONTHS ENDED NINE MONTHS ENDED SEPTEMBER 30, SEPTEMBER 30, --------------------- ----------------------- 2004 2003 2004 2003 --------- -------- --------- -------- (THOUSANDS OF DOLLARS, EXCEPT PERCENTS) Gross premium recognized on loan sales and securitizations .... $ 204,820 $ 123,116 $ 612,897 $ 321,154 Premium recapture and reversal .... (9,191) (2,791) (22,133) (7,864) --------- --------- --------- --------- Net premium recognized on loan sales and securitizations .... 195,629 120,325 590,764 313,290 Less: Direct costs of loan originations, net of fees received .... (90,321) (38,234) (230,474) (96,011) Adjustments to carrying value of loans held for sale .... (9,390) 1,609 (18,755) (5,674) Change in fair value of derivative instruments .... (6,552) - (2,923) - --------- --------- --------- --------- Gain on sale (GAAP) .... 89,366 83,700 338,612 211,605 Less: Origination expenses allocated during the period of origination .... (53,561) (21,653) (145,377) (60,086) --------- --------- --------- --------- Net operating gain on sale .... $ 35,805 $ 62,047 $ 193,235 $ 151,519 ========= ========= ========= ========= Gross premium recognized on loan sales and securitizations .... 3.02 % 4.42 % 3.68 % 4.39 % Premium recapture and reversal .... (0.14)% (0.10)% (0.13)% (0.11)% --------- --------- --------- --------- Net premium recognized on loan sales and securitizations .... 2.88 % 4.32 % 3.55 % 4.28 % Less: Direct costs of loan originations, net of fees received .... (1.32)% (1.37)% (1.39)% (1.31)% Adjustments to carrying value of loans held for sale .... (0.14)% 0.06 % (0.12)% (0.08)% Change in fair value of derivative instruments .... (0.10)% 0.00 % (0.02)% 0.00 % --------- --------- --------- --------- Gain on sale (GAAP) .... 1.32 % 3.01 % 2.02 % 2.89 % Less: Origination expenses allocated during the period of origination .... (0.79)% (0.78)% (0.88)% (0.82)% --------- --------- ---------- --------- Net operating gain on sale .... 0.53 % 2.23 % 1.14 % 2.07 % ========= ========= ========= ========= o Percentages are of total loan sales and securitizations, net of repurchases, during the period indicated. o Direct costs are costs directly incurred with the origination of the loans, net of loan fees received from borrowers, and which are deferred and recognized when the loans are sold. o Premium recapture and reversal represent the recapture or reversal of premium on loans sold which either prepay early per the terms of each sales contract or for certain loans repurchased from prior sales; includes some interest adjustment on loans repurchased. o Origination expenses represent indirect expenses related to the origination of residential real estate loans during the period of origination and which are not deferred for GAAP. These expenses are included in non-interest expense in the consolidated statement of operations during the period incurred. o Net operating gain on sale is a supplement to, and not a substitute for, the information presented in the consolidated statement of operations as prepared in accordance with GAAP. The Company utilizes this additional information as part of its management of the total costs and efficiency of its loan origination platform. Furthermore, our definition of the indirect origination expenses may not be comparable to similarly titled measures reported by other companies. The net operating gain on sale amount does not include net interest income on residential real estate loans held for sale or any fair value adjustments on the Company's residual interests in securitized loans. o The amount of gain on sale is significantly impacted by the timing of loan sales and securitizations. A number of factors influence the timing of loan sales and securitizations, including the current market pricing of the loans, liquidity requirements and other objectives. The sale or securitization of loans have, from time to time, been delayed to a later period, and may be so delayed in future periods. The Company's loan servicing income, before mortgage servicing rights amortization and impairment provision, increased from $2.5 million in the third quarter of 2003 to $11.7 million for the third quarter of 2004. For the first nine months of 2004 loan servicing income was $25.6 million versus $6.4 million for the first nine months of 2003. This increase was due to the significantly larger amount of residential real estate loans being serviced by the Company during 2004. The total amount of loans being serviced were $14.9 billion and $6.6 billion as of September 30, 2004, and 2003, respectively. 32 NON-INTEREST EXPENSE Non-interest expense increased during the third quarter and first nine months of 2004, as compared to the third quarter and first nine months of 2003. Compensation expense for the third quarter and first nine months of 2004 represented most of the change as it increased to $51.0 million for the third quarter of 2004 from $38.7 million in the third quarter of 2003 and to $186.2 million for the first nine months of 2004 from $113.5 million in the first nine months of 2003. Both increases are substantially a result of increased residential real estate loan origination volume (which increased 50% and 84% on a quarter-to-quarter and year-to-year comparative basis, respectively), which was a result, primarily, of increased staffing to originate and accommodate the higher loan origination volume, and to a lesser degree, an increase in staff to administer the increase in the loan servicing portfolio. To a lesser degree, other personnel and infrastructure costs increased. INCOME TAXES Income tax expense of $59.8 million and $39.0 million for the quarters ended September 30, 2004 and 2003, respectively, represents effective tax rates for both quarters of 41.3% on income before income taxes from continuing operations of $144.9 million and $94.5 million for the same respective periods. For the nine month periods ended September 30, 2004 and 2003, income tax expense was $186.5 million and $101.0 million, respectively. This represents effective tax rates of 41.5% and 41.2%, respectively, on income before income taxes from continuing operations of $449.6 million and $244.9 million for the same respective periods. The effective tax rates for all periods presented are different than the federal enacted tax rate of 35%, due mainly to various apportioned state income tax provisions resulting from the Company's nationwide lending operations. LOANS HELD FOR INVESTMENT AND SALE The Company's net loans held for investment before the allowance for loan losses, was approximately $3.86 billion at September 30, 2004, as compared to $4.79 billion and $4.65 billion at December 31, 2003 and September 30, 2003, respectively. The Company's residential real estate loans held for sale have increased from $3.10 billion at September 30, 2003 to $4.36 billion at September 30, 2004; this increase is reflective of a significant increase in loan production volume. During the third quarter of 2004, residential real estate loan originations totaled $5.88 billion as compared to $3.92 billion for the third quarter of 2003. During the first nine months of 2004, residential real estate loan originations totaled $16.87 billion as compared to $9.16 billion for the first nine months of 2003. 33 The following table shows detail for the Company's loans held for investment outstanding as of the dates indicated (in thousands of dollars): SEPTEMBER 30, DECEMBER 31, 2004 2003 ----------- ----------- Commercial real estate loans: Bridge .... $ 1,830,845 $ 1,659,847 Construction

.... 1,062,676 804,793 Permanent .... 794,956 1,281,877 Single tenant credit .... 196,494 268,506 ----------- ----------- 3,884,971 4,015,023 Residential real estate loans .... - 789,951 Syndicated commercial loans .... 3,013 6,857 Other .... 4,504 4,615 ----------- ----------- 3,892,488 4,816,446 Net deferred loan fees and origination costs .... (35,335) (25,436) ----------- ----------- 3,857,153 4,791,010 Allowance for loan losses .... (189,622) (213,591) ----------- ----------- Loans held for investment - net .... $ 3,667,531 $ 4,577,419 =========== =========== As of September 30, 2004, approximately 36.9% and 14.2% of the Company's commercial real estate loans outstanding were secured by properties located within California and New York, respectively; no other state represented greater than 10% of the loan portfolio. The Company's largest single individual commercial real estate loan outstanding at September 30, 2004 was $71.3 million with a total loan commitment of $84.0 million. The second largest loan, however, is cross-collateralized and cross-defaulted, with another loan that is sponsored by the same investment fund on a related real estate project. The combined loan principal outstanding and total loan commitment of these two loans at September 30, 2004 is $78.3 million and $81.9 million, respectively. The Company's largest net commitment for a single loan at September 30, 2004 was $109.5 million; this represents the maximum potential loan amount to the borrower. In addition, the commercial real estate loan portfolio's largest concentration by common investor or sponsor totaled $111.6 million in loan principal outstanding and $127.4 million in total loan commitment at September 30, 2004, and is comprised of two separate loans, each of which was performing as of September 30, 2004. 34 The following table stratifies the commercial real estate loans held for investment by loan amounts outstanding as of September 30, 2004 (in thousands of dollars, except percents and number of loans): NUMBER TOTAL LOANS LOAN SIZE RANGE OF LOANS OUTSTANDING % -------------------------- -------- ----------- --- $0 - $1 million .... 105 $ 20,872 1% > $1 million - $5 million .... 149 401,955 10% > $5 million - $10 million .... 98 720,395 19% > $10 million - $15 million .... 49 604,316 16% > $15 million - $20 million .... 22 367,862 9% > $20 million - $30 million .... 27 636,481 16% > $30 million - $40 million .... 14 499,135 13% > $40 million - $50 million .... 6 268,302 7% > $50 million .... 6 365,653 9% -------- ----------- --- 476 $ 3,884,971 100% ======== =========== === The following tables report the non-performing asset classifications, accruing loans past due 90 days or more, loan loss experience and allowance for loan losses reconciliation for the Company's loans held for investment as of, and for, the respective periods ended; the level of non-performing assets fluctuates and individual commercial real estate loans can have a material impact upon the total (thousands of dollars): SEPTEMBER 30, DECEMBER 31, 2004 2003 ------------ ----------- Non-accrual loans held for investment: Commercial real estate .... $ 64,242 $ 71,758 Residential real estate .... - 8,482 Syndicated commercial loans .... 2,908 6,752 ------------ ----------- $ 67,150 $ 86,992 ============ =========== Accruing commercial real estate loans past due 90 days or more .... $ - $ 36,406 ============ =========== Foreclosed real estate (REO): Commercial real estate .... $ 27,327 $ 23,621 Residential real estate .... 1,358 1,845 ------------ ----------- $ 28,685 $ 25,466 ============ =========== 35 THREE MONTHS ENDED SEPTEMBER 30, 2004 --- SYNDICATED COMMERCIAL RESIDENTIAL COMMERCIAL AND REAL ESTATE REAL ESTATE OTHER LOANS TOTAL ----------- ----------- --------------- --------- Beginning allowance for loan losses .... $ 191,518 $ 21,636 $ 1,572 $ 214,726 Provision for loan losses .... 1,707 (11,766) (250) (10,309) Charge-offs .... (5,353) (21) - (5,374) Charge-offs (fair value adjustment) .... - (9,856) - (9,856) Recoveries .... 392 7 36 435 ----------- ----------- --------------- --------- Net Charge-offs .... (4,961) (9,870) 36 (14,795) ----------- ----------- --------------- --------- Ending allowance for loan losses .... $ 188,264 $ - $ 1,358 $ 189,622 =========== =========== =============== ========= THREE MONTHS ENDED SEPTEMBER 30, 2003 --- SYNDICATED COMMERCIAL RESIDENTIAL COMMERCIAL AND REAL ESTATE REAL ESTATE OTHER LOANS TOTAL ----------- ----------- --------------- --------- Beginning allowance for loan losses .... $ 180,013 $ 9,055 $ 2,037 $ 191,105 Provision for loan losses .... 25,934 3,441 32 29,407 Charge-offs .... (14,000) (81) - (14,081) Recoveries .... 569 38 - 607 ----------- ----------- --------------- --------- Net

Charge-offs .... (13,431) (43) - (13,474) ----------- ----------- -------------- --------- Ending allowance for loan losses .... $ 192,516 $ 12,453 $ 2,069 $ 207,038 =========== =========== =============== ========= 36 NINE MONTHS ENDED SEPTEMBER 30, 2004 -- SYNDICATED COMMERCIAL RESIDENTIAL COMMERCIAL AND REAL ESTATE REAL ESTATE OTHER LOANS TOTAL ----------- ----------- -------------- --------- Beginning allowance for loan losses .... $ 195,000 $ 15,607 $ 2,984 $ 213,591 Provision for loan losses .... 12,255 (5,463) (556) 6,236 Charge-offs .... (19,519) (403) (1,236) (21,158) Charge-offs (fair value adjustment) .... - (9,856) - (9,856) Recoveries .... 528 115 166 809 ----------- ----------- -------------- --------- Net Charge-offs .... (18,991) (10,144) (1,070) (30,205) ----------- ----------- -------------- --------- Ending allowance for loan losses .... $ 188,264 $ - $ 1,358 $ 189,622 =========== =========== ============== ========= NINE MONTHS ENDED SEPTEMBER 30, 2003 -- SYNDICATED COMMERCIAL RESIDENTIAL COMMERCIAL AND REAL ESTATE REAL ESTATE OTHER LOANS TOTAL ----------- ----------- -------------- --------- Beginning allowance for loan losses .... $ 147,227 $ 7,844 $ 6,119 $ 161,190 Provision for loan losses .... 79,032 4,823 (3,919) 79,936 Charge-offs .... (34,312) (315) (199) (34,826) Recoveries .... 569 101 68 738 ----------- ----------- -------------- --------- Net Charge-offs .... (33,743) (214) (131) (34,088) ----------- ----------- -------------- --------- Ending allowance for loan losses .... $ 192,516 $ 12,453 $ 2,069 $ 207,038 =========== =========== =============== ========= Non-accrual loans held for investment were $67.2 million as of September 30, 2004. This is 1.74% of the total loans held for investment as of September 30, 2004. This is compared to $87.0 million in total non-accrual loans as of December 31, 2003, which was 1.82% of the total loans held for investment as of that date. As of September 30, 2004, $64.2 million of the total $67.2 million in non-accrual loans were related to the commercial real estate portfolio. The $64.2 million was comprised of 14 non-accrual loans (the largest having a balance of $15.5 million). Total REO was $28.7 million at September 30, 2004, as compared to $25.5 million at December 31, 2003. Commercial real estate REO at September 30, 2004 was comprised of 11 properties, the largest having a balance of $7.2 million. The Company maintains an allowance for losses on REO, which is detailed as follows (thousands of dollars): AS OF SEPTEMBER 30, 2004 AS OF DECEMBER 31, 2003 -------------------------------------- -------------------------------------- COMMERCIAL RESIDENTIAL COMMERCIAL RESIDENTIAL REAL ESTATE REAL ESTATE TOTAL REAL ESTATE REAL ESTATE TOTAL ----------- ----------- -------- ----------- ----------- -------- REO .... $ 27,703 $ 1,488 $ 29,191 $ 26,465 $ 2,016 $ 28,481 Allowance for losses .... (376) (130) (506) (2,844) (171) (3,015) ----------- ----------- -------- ----------- ----------- -------- REO - net .... $ 27,327 $ 1,358 $ 28,685 $ 23,621 $ 1,845 $ 25,466 =========== =========== ======== =========== =========== ======== 37 The allowance for loan losses, as a percentage of total loans held for investment increased to 4.92% as of September 30, 2004, as compared to 4.50% at June 30, 2004. Total net charge-offs in the third quarter of 2004 totaled $14.8 million, as compared to $13.5 million for the third quarter of 2003. The net charge-offs for the third quarter of 2004 were comprised of $9.9 million related to the residential real estate portfolio transfer to held for sale, with the remaining balance related to commercial real estate loans. For the third quarter of 2003 the net charge-offs were substantially all related to commercial real estate loans. During the third quarter of 2004, there were no commercial real estate loans restructured as to their terms and included in accrual status at September 30, 2004. During the third quarter of 2003, there were eight loans that were restructured and included in accrual status. The following table shows detail for the Company's residential real estate loans held for sale as of the dates indicated: SEPTEMBER 30, DECEMBER 31, 2004 2003 ------------ ----------- (THOUSANDS OF DOLLARS) Residential real estate loans held for sale: Loan principal outstanding: First trust deeds .... $ 4,069,089 $ 3,466,432 Second trust deeds .... 273,197 160,855 ------------ ------------ 4,342,286 3,627,287 Deferred origination costs, net of loan fees received .... 60,859 50,067 Valuation reserve .... (41,725) (23,807) ------------ ------------ Residential real estate loans held for sale - net .... $ 4,361,420 $ 3,653,547 ============ =========== Non-accrual residential real estate loans held for sale ("HFS") .... $ 18,830 $ 6,253 ============ =========== The increase in residential real estate loans held for sale is a result of significantly increased loan origination volume. The following table details residential real estate loan origination for the respective periods indicated (thousands of dollars): THREE MONTHS ENDED NINE MONTHS ENDED

SEPTEMBER 30, SEPTEMBER 30, -------------------------- --------------------------- 2004 2003 2004 2003 ----------- ----------- ------------ ----------- Loan originations: First mortgage .... $ 5,515,901 $ 3,728,558 $ 15,951,462 $ 8,738,805 Second mortgage .... 369,076 186,748 918,111 424,994 ----------- ----------- ------------ ----------- $ 5,884,977 $ 3,915,306 $ 16,869,573 $ 9,163,799 =========== =========== ============ =========== 38 THREE MONTHS ENDED NINE MONTHS ENDED SEPTEMBER 30, SEPTEMBER 30, ---------------------- ------------------------ 2004 2003 2004 2003 ----------- --------- --------- ---------- (THOUSANDS OF DOLLARS, EXCEPT PERCENTS) FIRST MORTGAGES - ORIGINATION: TYPE OF PRODUCT: Adjustable Rate (2/28) .... 83.9% 69.0% 78.1% 72.4% Adjustable Rate (3/27) .... 3.7% 2.6% 4.0% 1.7% Adjustable Rate (5/25) .... 1.4% 0.0% 0.5% 0.0% Fixed .... 11.0% 28.4% 17.4% 25.9% --------- --------- --------- --------- 100.0% 100.0% 100.0% 100.0% ========= ========= ========== ========= PURPOSE: Refinance .... 54.3% 59.1% 57.7% 61.8% Purchase .... 45.7% 40.9% 42.3% 38.2% --------- --------- --------- --------- 100.0% 100.0% 100.0% 100.0% ========= ========= ========== ========= Average Loan Size .... $ 210,515 $ 201,011 $ 209,869 $ 194,958 Average FICO Score .... 614 629 619 623 Average LTV .... 80.4% 81.7% 81.0% 81.2% FIRST & SECOND MORTGAGES - ORIGINATION: GEOGRAPHIC DISPERSION: California .... 31.9% 45.2% 35.6% 43.9% New York .... 11.5% 8.8% 11.3% 8.6% New Jersey .... 7.6% 4.1% 6.0% 4.2% Florida .... 7.2% 7.9% 7.6% 8.9% Illinois .... 5.6% 5.1% 5.4% 4.9% All other states .... 36.2% 28.9% 34.1% 29.5% --------- --------- --------- --------- 100.0% 100.0% 100.0% 100.0% ========= ======== ========= ========= LIQUIDITY AND CAPITAL RESOURCES FIL finances its lending activities primarily through Federal Deposit Insurance Corporation ("FDIC") insured customer deposits, which totaled $7.3 billion at September 30, 2004. FIL is also eligible for financing through the Federal Home Loan Bank of San Francisco ("FHLB"), for which financing is available to FIL based upon advance rates on certain pledged collateral and at various rates and terms. At September 30, 2004, FIL had borrowing capacity with the FHLB of $2.49 billion, of which $727 million was borrowed and outstanding. The $2.49 billion in borrowing capacity was based upon a total of $2.82 billion in pledged loan collateral at September 30, 2004. FIL's maximum financing availability, based upon its regulatory assets and subject to the amount of collateral pledged and their related advance rates, was approximately $3.6 billion. 39 As of September 30, 2004, FIL had three separate warehouse lines of credit in place for the funding of residential real estate loans prior to their sale or securitization. The total funding capacity of these three facilities was $1.5 billion at September 30, 2004. Borrowings, if any, under each of the facilities are secured by loans held for sale as pledged by FIL. There were no amounts outstanding at September 30, 2004. The three facilities are summarized as follows: o $500 million master loan and security facility ($250 million committed) with Greenwich Capital Financial Products expiring in September 2005, interest at one-month LIBOR plus a margin of 0.50%. o $500 million master repurchase facility ($250 million committed) with Credit Suisse First Boston Mortgage Capital expiring in January 2005, interest at overnight LIBOR plus a margin of 0.50%. o $500 million master repurchase facility ($250 million committed) with Goldman Sachs Mortgage Company expiring in December 2004, interest at one-month LIBOR plus a margin of 0.50%. Each of the facilities is subject to certain conditions, including but not limited to financial and other covenants. At September 30, 2004, FIL was in compliance with all financial and other covenants under these facilities. The Company expects to renew its Credit Suisse First Boston and Goldman Sachs facilities prior to their expiration. In addition, FIL has a line of credit with the Federal Reserve Bank of San Francisco ("FRB") with a borrowing capacity of $250.5 million at September 30, 2004. There were no amounts outstanding under the line of credit with the FRB at September 30, 2004. The Company's residential loan disposition strategy is to primarily utilize both whole loan sales and, to a lesser extent, securitizations. The Company attempts to build multiple whole loan sale relationships to achieve diversity and enhance market liquidity. During the first nine months of 2004, the Company had transacted whole loan sales with 22 different financial institutions, the largest institution representing 21.7% of the total whole loan sales volume during this period. The FDIC has established certain capital and liquidity standards for its member institutions and FIL was in compliance with these standards as of September 30, 2004. As a holding company, Fremont General pays its operating expenses, interest expense, taxes and stockholders' dividends, and meets its other obligations primarily from its cash on hand and intercompany tax payments from FIL. Dividends of $4.6 million and $2.2 million were paid on Fremont General's common stock in the quarters ending September 30, 2004 and 2003, respectively; however, no assurance can be given that future common stock dividends will be declared. 40 During 2003, Fremont General had significant net operating loss carryforwards which were used to offset taxable income generated by FIL. As a result, intercompany payments of federal income tax obligations from FIL, which were otherwise payable to taxing authorities, were available for use by Fremont General for general working capital purposes. The last of the net operating loss carryforwards were fully utilized during 2003 and only current operating losses at Fremont General will offset taxable income generated by FIL; as a result, beginning in 2004, Fremont General is expected to pay most of the federal income taxes it receives from FIL to the federal taxing authorities. There exist certain tax matters from prior years that are in various processes of resolution or determination. The matters primarily relate to the deduction of certain expenses and losses at the holding company. A reserve in the amount of $38.9 million exists at September 30, 2004 for the expected maximum tax and interest for these potential exposures; however, the final resolution of these matters, which is expected to take several years, may be for a lesser amount, possibly significantly lower, depending upon various administrative outcomes. Fremont General does not believe that the actual outcomes of these potential exposures will adversely impact its liquidity. Fremont General has cash and cash equivalents of $142.0 million at September 30, 2004 and no debt maturities until March of 2009. ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK The Company is subject to market risk resulting primarily from fluctuations in interest rates arising from balance sheet financial instruments such as investments, loans (both held for investment and for sale) and debt. Changes, and the timing thereof, in interest rates will affect the Company's net investment income, loan interest, net gain on sale of residential real estate loans, interest expense and total stockholders' equity. The level of net gain on sale of residential real estate loans is highly dependent upon the level of loan origination volume and the net premium paid by the purchasers of such loans. Both the volume and net premium, in turn, are highly dependent upon changes in, and the level of, interest rates and other economic factors. The Company may experience a decrease in the amount of gain it realizes should significant interest rate increases occur or if other economic factors have a negative impact on the value and volume of the loans the Company originates. The objective of the Company's asset and liability management activities is to provide the highest level of net interest and investment income and to seek cost effective sources of capital, while maintaining acceptable levels of interest rate and liquidity risk. It is not the Company's policy to utilize derivative instruments as a means to speculate on interest rates. As part of its residential real estate mortgage banking operations, the Company enters into commitments to originate loans ("interest rate lock commitments"), which represent commitments that have been extended by the Company, generally for a period of 30 days, at a stated interest rate to its potential borrowers. Typically, the Company hedges the risk of overall changes in the fair value for its loans held for sale through entering into forward loan sale commitments and interest rate cap contracts. The Company determined that certain of its interest rate lock commitments, forward sales commitments and interest rate cap contracts have met the definition of derivatives under SFAS No. 133, "Accounting for Derivative 41 Instruments and Hedging Activities"; and records them at their estimated fair value. The Company may in the future utilize other derivative instruments as part of its risk management program. Quantitative and qualitative disclosures about the Company's market risk are included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2003. There have been no material changes in such risks or in the Company's asset and liability management activities during the nine months ended September 30, 2004. ITEM 4. CONTROLS AND PROCEDURES As of September 30, 2004, the Company evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures. The evaluation was performed under the supervision and with the participation of the Company's management, including the Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"). Based on that evaluation, the Company's management, including the CEO and CFO, and its audit committee, have concluded that the Company's disclosure controls and procedures were effective as of September 30, 2004. There have been no changes in the Company's internal controls over financial reporting that occurred in the last fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting. The Company has begun a detailed assessment of its internal and financial disclosure controls as required by the Sarbanes-Oxley Act of 2002. Although the Company has made this project a top priority, there can be no assurances that any control deficiencies identified and validated will be remediated before the end of the Company's fiscal year or that any remaining unresolved control deficiencies will not rise to the level of significant deficiencies or material weaknesses. 42 PART II - OTHER INFORMATION ITEM 2: UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS ISSUER PURCHASES OF EQUITY SECURITIES

-- (c) TOTAL NUMBER (d) MAXIMUM NUMBER (a)TOTAL OF SHARES (OR UNITS) (OR APPROXIMATE DOLLAR NUMBER OF (b) AVERAGE PURCHASED AS PART VALUE) OF SHARES (OR SHARES PRICE PAID OF PUBLICLY UNITS) THAT MAY YET BE (OR UNITS) PER SHARE ANNOUNCED PLANS PURCHASED UNDER THE PERIOD PURCHASED (1) (OR UNIT) (1) OR PROGRAMS PLANS OR PROGRAMS ---------------------------------- ------------ ----------- ------------------ --------------------- July 1-31, 2004 90,840 $0
-- August 1-31, 2004 - -

September 1-30, 2004 38,500 $0
-- Total 129,340 $0
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(1) Reflects restricted shares of common stock with unlapsed restrictions that were reacquired by the Company at a cost of $0 upon termination of employment by the participant, under the terms of the 1995 Restricted Stock Award Plan and/or 1997 Stock Plan pursuant to which the shares were initially awarded. ITEM 6: EXHIBITS EXHIBIT NO. DESCRIPTION ----------- --- 3.1 Restated Articles of Incorporation of Fremont General Corporation. (Incorporated by reference to Exhibit 3.1 to the Registrant's Quarterly Report on Form 10-Q, for the period ended June 30, 1998, Commission File Number 1-8007.) 3.2 Certificate of Amendment of Articles of Incorporation of Fremont General Corporation. (Incorporated by reference to Exhibit 3.2 to the Registrant's Annual Report on Form 10-K, for the fiscal year ended December 31, 1998, Commission File Number 1-8007.) 3.3(a) Amended and Restated Bylaws of Fremont General Corporation. (Incorporated by reference to Exhibit 3.3 to the Registrant's Annual Report on Form 10-K, for the fiscal year ended December 31, 1995, Commission File Number 1-8007.) 3.3(b) Fremont General Corporation Bylaw Amendment Adopted by the Board of Directors on November 30, 2003. (Incorporated by reference to Exhibit 3.3(b) to the Registrant's Annual Report on Form 10-K, for the fiscal year ended December 31, 2003, Commission File Number 1-8007.) 3.3(c) Fremont General Corporation Bylaw Amendment Adopted by the Board of Directors on March 16, 2004. (Incorporated by reference to Exhibit 3.1 to the Registrant's Quarterly Report on Form 10-Q, for the period ended June 30, 2004, Commission File Number 1-8007.) 4.1 Form of Stock Certificate for Common Stock of the Registrant. (Incorporated by reference to Exhibit 4.1 to the Registrant's Annual Report on Form 10-K, for the fiscal year ended December 31, 2000, Commission File Number 1-8007.) 43 EXHIBIT NO. DESCRIPTION ----------- --- 4.2 Indenture with respect to Liquid Yield Option Notes Due 2013 between the Registrant and Bankers Trust Company. (Incorporated by reference to Exhibit 4.4 to the Registrant's Registration Statement on Form S-3 filed on October1, 1993, Registration Number 33-68098.) 4.3 Indenture among the Registrant, the Trust and Bank of New York (originated with First Interstate Bank of California), a New York Banking Corporation, as trustee. (Incorporated by reference to Exhibit 4.3 to the Registrant's Annual Report on Form 10-K, for the fiscal year ended December 31, 1995, Commission File Number 1-8007.) 4.4 Amended and Restated Declaration of Trust among the Registrant, the Regular Trustees, The Chase Manhattan Bank (USA), a Delaware banking corporation, as Delaware trustee, and The Chase Manhattan Bank, N.A., a national banking association, as Institutional Trustee. (Incorporated by reference to Exhibit 4.5 to the Registrant's Annual Report on Form 10-K, for the fiscal year ended December 31, 1995, Commission File Number 1-8007.) 4.5 Preferred Securities Guarantee Agreement between the Registrant and The Chase Manhattan Bank, N.A., a national banking association, as Preferred Guarantee Trustee. (Incorporated by reference to Exhibit 4.6 to the Registrant's Annual Report on Form 10-K, for the fiscal year ended December 31, 1995, Commission File Number 1-8007.) 4.6 Common Securities Guarantee Agreement by the Registrant. (Incorporated by reference to Exhibit 4.7 to the Registrant's Annual Report on Form 10-K, for the fiscal year ended December 31, 1995, Commission File Number 1-8007.) 4.7 Form of Preferred Securities. (Included in Exhibit 4.5). (Incorporated by reference to Exhibit 4.8 to the Registrant's Annual Report on Form 10-K, for the fiscal year ended December 31, 1995, Commission File Number 1-8007.) 31.1 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. 31.2 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. 32.1 Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. 32.2 Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

With respect to long-term debt instruments, the Registrant undertakes to provide copies of such agreements upon request by the Commission. 44 SIGNATURES Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized. FREMONT GENERAL CORPORATION Date: November 8, 2004 /s/ LOUIS J. RAMPINO -- Louis J. Rampino President and Chief Executive Officer Date: November 8, 2004 /s/ PATRICK E. LAMB -- Patrick E. Lamb Senior Vice President, Chief Financial Officer and Treasurer (Principal Accounting Officer) 45